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Supreme Court of the United States

OCTOBER TERM, 1954

No. 45

FEDERAL POWER COMMISSION, PETITIONER,

vs.

COLORADO INTERSTATE GAS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

PETITION FOR CERTIORARI FILED APRIL 23, 1954
CERTIORARI GRANTED JUNE 7, 1954

SUPREME COURT OF THE UNITED STATES

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INDEX

	Original	Print
Proceedings in the U.S.C.A. for the Tenth Circuit	1	1
Petition to review and set aside an order of the Federal Power Commission	1	1
Proceedings before the Federal Power Commission	10	9
Order instituting rate investigation	10	9
Notice of intervention and petition for intervention, City and County of Denver (omitted in printing)	12	
Order fixing date of hearing (omitted in printing)	17	
Notice of intervention, Public Utilities Commission, State of Colorado (omitted in printing)	18	
Extract from minutes of meeting, Federal Power Commission, October 1, 1951	20	11
Motion for finding that staff has failed to meet the burden of proof	20	12
Motion for finding that staff has failed to show a case, etc.	24	15

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—7095

Proceedings before the Federal Power Commission—Continued	Original	Print
Notice of continuance of hearing	30	21
Order reconvening hearing	31	21
Motion to continue hearing	32	22
Notice of continuance of hearing	33	23
Appeal from ruling of presiding examiner	33	23
Answer to appeal from ruling of presiding examiner	39	29
Order on appeal from ruling of presiding examiner	43	33
Application for reconsideration and rehearing (omitted in printing)	44	
Order denying application for rehearing (omitted in printing)	57	
Motion to omit intermediate decision procedure or for issuance of tentative decision	57	34
Answer to motion to omit intermediate decision procedure or for issuance of tentative decision	59	36
Extract from Administrative Procedure Act, Section 8(a) (omitted in printing)	64	
Order omitting intermediate decision procedure and fixing date for oral argument	66	41
Presiding examiner's certification of record of hearing (omitted in printing)	69	
Application for rehearing of order omitting intermediate decision procedure	75	44
Opinion, No. 235, findings and order reducing rates	77	47
Tables—Colorado Interstate Gas Company—Year 1952	110	77
I—Computation of Percentages Used to Allocate Joint Gas & Gasoline Costs to Dry Gas and Natural Gasoline	110	77
—Allocation of Costs to Gasoline Operations and Computation of Net Loss Thereon	113	78
I—Excess Revenues and Cost of Service—By Functions	125	88
Tables	127	89
II—Summary—Allocation of Cost of Service, Total System	127	89
III—Allocation of Cost of Service—Production System	129	90
IV—Allocation of Cost of Service—Transmission System	131	91
V—Allocation of Cost of Service—Distribution System	135	93
Petition for rehearing, vacation and modification (Excerpts from)	141	97
A—Specifications of errors (Excerpts from)	142	97
C—Grounds relied upon (Excerpts from)	159	104

	Original	Print
Proceedings before the Federal Power Commission—Continued		
Opinion, No. 235 A, and order on petition for rehearing	188	118
Table I—Determination of Joint Well Mouth and Gathering Costs—Year 1952	201	130
Table II—Determination of Joint Gas and Gasoline Costs, Direct Gasoline Costs, and Direct Dry Gas Costs for Bivins and Fourway—Year 1952	203	130
Supplement to prospectus dated April 2, 1952 (Stipulation)	205	131
Transcript of hearing	206	131
Testimony of—		
W. Floyd Spurrier (omitted in printing)	206	
A. Alexander Wiskup	207	131
Dale E. Goubleman (resumed) (omitted in printing)	209	
Colloquy between Examiner and Counsel	211	131
Testimony of—		
William F. Spurrier (recalled)	220	140
Frank S. French (recalled)	238	157
Benjamin Schiffer (recalled) (omitted in printing)	243	
Jams D. Jones (omitted in printing)	245	
Eugene S. Merrill (recalled) (omitted in printing)	245	
Thomas L. Pelican (recalled) (omitted in printing)	246	
J. D. Jones (recalled) (omitted in printing)	247	
Alexander E. Wiskup (recalled)	249	161
William F. Spurrier (recalled)	265	173
Frederick J. Bucher (recalled) (omitted in printing)	268	
Frank S. French (recalled)	283	174
Alexander E. Wiskup (recalled)	286	177
W. F. Spurrier (recalled) (omitted in printing)	296	
James V. O'Connor (omitted in printing)	304	
V. A. McElfresh (omitted in printing)	314	
James V. O'Connor (resumed) (omitted in printing)	316	
Transcript of oral argument	317	188
Appearances	318	188
Certificate of the Secretary of the Commission	318	188
Argument on behalf of Federal Power Commission by Mr. Goldberg	319	189

	Original	Print
Proceedings before the Federal Power Commission—Continued		
Transcript of oral argument—Continued		
Argument on behalf of Colorado Interstate Gas Company by Mr. James L. White	338	206
Rebuttal argument by Mr. Goldberg	367	227
Exhibits	365	231
No. 1		
Schedule 3—Statement reflecting Staff's computation of Federal income tax giving effect to merger, year ended June 30, 1951	365	231
Schedule 8—Balance sheets giving effect to merger as at June 30, 1950 and 1951	367	232
Nos. 2 & 3 (omitted in printing)	369	
No. 11		
Page 12—List of Natural gas common stocks offered to public during period 1935 to date, etc.	383	233
Page 13—Earnings-price ratio of outstanding common stocks of seven natural gas companies, January, 1940 to date	387	235
Page 13a—Earnings-price ratio and yields on seven natural gas pipe line company common stocks, July 31, 1951	389	236
No. 13		
Schedule A (omitted in printing)	391	
Schedule B—Return at assumed rate of 6% based on estimates of Colorado Interstate Gas Co. etc. (Excerpts from)	393	237
Exhibits	399	237
Schedules C, D & E (omitted in printing)	399	
No. 18		
Tabulation showing allocation-excess earnings	405	238
Nos. 19 & 20 (omitted in printing)	407	
No. 21		
Schedule 1—Estimated cost of service and excess revenues, year 1952	411	239
Schedule 13 (omitted in printing)	413	
No. 23 (omitted in printing)	415	
No. 26		
Schedule A-1, Estimated excess revenues and cost of service, etc	417	240
Schedules A-5.1 & A-5.2 (omitted in printing)	419	240
Schedule A-7—Staff adjustment of return-year 1952	425	241
Schedules A-8, A-9, A-21 (omitted in printing)	427	241
No. 27 (omitted in printing)	433	

	Original	Print
Proceedings before the Federal Power Commission—Continued		
Exhibits—Continued		
No. 28		
Table No. 11, Summary, allocation of cost of service, total system, year 1952, estimated	437	242
No. 30		
Schedule No. 1—Estimated Cost of Service and Deficiency in Revenues as estimated for year 1952	441	242
Schedules Nos. 2-14 incl. (omitted in printing)	443	
Nos. 32, 33, 34, 35, 37, 39, 41, 43 (omitted in printing)	497	
Item A—Opinion, No. 209, Federal Power Commission, Docket No. G-1326	549	243
Dissenting opinion, Buchanan, Commissioner	562	256
Order issuing certificate of Public Convenience and Necessity authorizing acquisition and operation of pipeline facilities, etc.	564	257
Items C, M (omitted in printing)	568	
Certificate of Secretary of Federal Power Commission (omitted in printing)	592	
Argument and submission	593	262
Opinion, Huxman, J.	593	262
Concurring opinion, Bratton, J.	609	278
Judgment	610	279
Petition for rehearing of Federal Power Commission, respondent	610	279
Appendix A—Letter dated June 8, 1950 from Wm. A. Dougherty to Hon. Mon C. Wallgren	620	289
Order granting petition for rehearing	621	290
Argument and submission on rehearing	621	290
Cross-petition for rehearing of Colorado Interstate Gas Company, petitioner	622	291
Order denying petitioner's petition for rehearing	630	299
Opinion on rehearing, Huxman, J.	630	299
Judgment	633	302
Order re deposit in escrow account	633	302
Stay order	634	303
Clerk's certificate	635	304
Brief of petitioner in response to respondent's petition for rehearing	637	305
Appendix A—Excerpt, transcript of testimony, F. P. C. Docket G-1326, pp. 1008-1013)	654	322
Order extending time to file petition for writ of certiorari	659	327
Order allowing certiorari	663	327

[fol. 1]

IN THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

No. 4541

COLORADO INTERSTATE GAS COMPANY, Petitioner,

vs.

FEDERAL POWER COMMISSION, Respondent

PETITION TO REVIEW AND SET ASIDE AN ORDER OF THE FEDERAL POWER COMMISSION—Filed October 7, 1952

To the Honorable, the Judges of said Court:

Colorado Interstate Gas Company (hereinafter sometimes referred to as "Petitioner"), being aggrieved by an order of the Federal Power Commission (hereinafter sometimes referred to as the "Commission") issued August 8, 1952, respectfully petitions this Honorable Court to review and set aside said order, and in support of its petition alleges the following:

A.

JURISDICTION AND VENUE

Petitioner is a corporation organized and existing under the laws of the State of Delaware. It owns and operates a transmission natural gas pipe line system extending from the Panhandle Gas Field in Texas to a point near the City of Denver in the State of Colorado, and from a point near Lakin, Kansas, to the City of Denver. Petitioner maintains its principal office and place of business at Colorado Springs, Colorado. Petitioner has been and is now a "natural-gas company" within the meaning of the Natural Gas Act.

This petition for review is filed under and pursuant to the provisions of Section 19(b) of the Natural Gas Act of June

21, 1938 (52 Stat. 831) U. S. C. Title 15, §717r, which provides in part as follows:

[fol. 2] "Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part."

Petitioner filed a Petition for Rehearing, Vacation and Modification of the Commission's order within the time required by law, to wit, on August 27, 1952. This application was denied by the Commission by order adopted and stated to be effective September 26, 1952 but issued September 29, 1952.

B.

THE NATURE OF THE PROCEEDINGS OF WHICH REVIEW IS SOUGHT

The order of the Commission brought here for review is one reducing Petitioner's rates on the sale of natural gas in interstate commerce for resale. This order was issued by the Commission in its Docket G-1115 on August 8, 1952 accompanied by its Opinion No. 235 and resulted in a finding that the rates of Petitioner for the sale of natural gas in interstate commerce for resale were excessive and should be reduced by not less than $3,111,187 based upon the test year 1952.

The proceeding originally was instituted by the Commission on September 2, 1948 pursuant to Section 5 of the Natural Gas Act (15 U. S. C., §717d) to determine whether any rate, charge, service or classification observed, charged or collected by Canadian River Gas Company and Colorado Interstate Gas Company for or in connection with the transportation or sale of natural gas subject to the Commission's

jurisdiction was unjust, unreasonable, unduly discriminatory or preferential. The proceeding now is being carried on by Colorado Interstate Gas Company as the sole Petitioner since Canadian River Gas Company was merged into Colo- [fol. 3] rado Interstate Gas Company on December 28, 1951 and the order of the Commission of which review is sought is solely against this Petitioner. Hearings were held at various sessions before a Presiding Trial Examiner of the Commission beginning October 1, 1951 and concluding on April 4, 1952. Subsequent to the filing of main briefs addressed to the Trial Examiner and on the same day that reply briefs were filed, the Commission issued an order on May 26, 1952 taking the case away from the Trial Examiner for his initial decision and requiring that the case be presented to the Commission en banc by oral argument on June 9, 1952. Although there were intervenors* in the Commission proceeding, the Commission Staff and Petitioner were the only ones who offered evidence, filed briefs or participated in the oral argument before the Commission.

Within the period of thirty days, after the issuance of the Commission's said opinion and order allowed by Section 19 of the Natural Gas Act (15 U. S. C. §717r), Petitioner on August 27, 1952 filed its Petition for Rehearing Vacation and Modification of the Commission's Order. On August 27, 1952 Petitioner also filed with the Commission a Motion for Stay of the Commission's Order issued August 8, 1952.

On September 8, 1952 Petitioner applied to this Honorable Court for a Stay Pending Review of the Rate Order of the Commission which is the subject of this review, and this Court by its order entered the same day granted a stay.

The Commission by order dated September 26, 1952 and issued September 29, 1952 denied Petitioner's Petition for Rehearing, Vacation and Modification of the Commission's

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*The City of Denver, Colorado; the City of Colorado Springs, Colorado; Public Service Company of Colorado; Public Utilities Commission of the State of Colorado; and Natural Gas Pipeline Company of America.

Order. (A copy of this order is attached hereto as Exhibit "D")*

[fol. 4] C.

POINTS UPON WHICH PETITIONER INTENDS TO RELY

In prosecuting this review Petitioner will rely upon the following points, all of which are within the purview of the application made to the Respondent Commission for rehearing:

1. The Commission erred in the proceedings before it in denying to Petitioner due process of law to which Petitioner was entitled under the provision of the Constitution (Amendment V), the Administrative Procedure Act (5 U. S. C. §1001-1011), the Natural Gas Act (15 U. S. C. §717), and other applicable law:

a. In failing to give due and timely notice of the claims asserted against Petitioner and of the bases for the Commission's action, so as to permit Petitioner fully to meet and answer the claims, contentions and bases so put in issue. Specifically, the Commission Staff presented five cases-in-chief against Petitioner and at no time prior to the filing of the Staff's initial brief was Petitioner able to ascertain the claims which the Commission Staff were asserting against it, although, as the record will show, Petitioner diligently tried to ascertain such facts.

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*Prior exhibits have been filed with this Court as attachments to Petitioner's Petition for Stay Pending Review of Rate Order as follows:

Exhibit A—Order of Federal Power Commission, Opinion No. 235, dated July 31, 1952, issued August 8, 1952, Docket No. G-1115.

Exhibit B—Petition of Colorado Interstate Gas Company for Rehearing, Vacation and Modification, filed with the Federal Power Commission, August 27, 1952.

Exhibit C—Motion of Colorado Interstate Gas Company for Stay, filed with the Federal Power Commission, August 27, 1952.

b. In interfering with the course of the hearings before the Commission's Trial Examiner in such manner as to deprive Petitioner of its right to a fair hearing. Specifically, the Commission interfered with the recesses granted by the Trial Examiner after said Examiner weighed all relevant facts as to the time required during recess to prepare for cross-examination of Staff witnesses by Petitioner. Further, the Commission made no findings that the time allowed by the Examiner was excessive or that he had abused his discretion in the premises but, nevertheless, in the recess period itself shortened the period of time within which Petitioner could prepare for the cross-examination of Staff witnesses and the presentation of countervailing evidence.

c. In ordering the omission of the intermediate decision procedure and taking the case from the Trial Examiner, so as to further deny to Petitioner its right to a fair hearing. The record in this case does not support such action and [fol. 5] clearly indicates that the issues of fact were sharply drawn and that the proceeding was accusatory in nature. The record also shows that important determinations of fact had to be made wherein the credibility of evidence and witnesses would be an important factor. It was, therefore, error for the Commission to take the case from the Presiding Officer who is in position to evaluate evidence in the light of demeanor of witnesses and other factors affecting credibility. The order of the Commission taking the case from the Trial Examiner was issued May 26, 1952 although dated May 23, 1952. May 26, 1952 was the date final briefs to the Examiner were due. The effect of the Commission's order of omission, therefore, was to deprive Petitioner of its right to brief and argue its cause. The effect of the Commission's action in omitting the intermediate decision procedure also deprived this Petitioner of an important portion of the record in this case.

d. In making an adjustment to the working capital allowance contrary to all of the evidence of record and without notice at any time of the fact that such adjustment was contemplated. The adjustment made by the Commission is in the amount of $139,199 because under the Commission's rationale advance collection of Federal income taxes would supply working capital in this amount. Working capital in

the record was computed upon the basis used in the past by the Commission and there was no possible indication prior to the order of the Commission that any other method would be used in this case. The Commission by failing to give notice of this fact during hearing effectively deprived Petitioner of its right to introduce its own contentions in respect of such proposed adjustment either by way of showing the inadequacy of such working capital allowance or other factors which should be weighed in determining a proper working capital allowance.

2. The Commission erred in disallowing certain expenses and taxes from Petitioner's estimated 1952 cost of service upon which the Commission's rate order was based, as follows:

a. In adjusting Federal income taxes by the amount of $1,037,679 for the year 1952 by the use of a deduction for percentage depletion based upon a wellhead value of gas of [fol. 6] 5¢ per M.c.f.* for all of the gas produced from Petitioner's acreage in the West Panhandle Field in Texas. The Commission in so acting has improperly assumed a conclusion which must be made by another independent agency of the Federal Government. In fact, the last allowance of the Bureau of Internal Revenue in this regard was based upon a wellhead value of gas of 3.17¢ per M.c.f. Subsequent to the close of the record in this proceeding, Petitioner received a letter from the Bureau of Internal Revenue showing that the conclusion of the Commission is unwarranted at this time and noting the fact that no conclusion could be reached in respect of the wellhead value until subsequent to the end of 1952 and, further, noting that no reasonable basis for estimating such value could be made at this time. This letter was Exhibit B to Petitioner's Petition for Rehearing, Vacation and Modification of the Commission's Order in this case and is also Exhibit B to Petitioner's Petition for a Stay in this docket. Petitioner, pursuant to the rules of the Commission, proffered such evidence as a ground for modification of the order of which review is sought herein. It was error, therefore, for the Commission not to consider this

*1,000 cubic feet.

evidence and modify its findings so as to comport with the facts.

b. The Commission erred in reducing the cost of service for the year 1952 in the amount of $421,537 which it alleges to be a loss Petitioner will incur in the operation of gasoline extraction plants in the West Panhandle Field of Texas which loss, under the terms of a previous order entered by the Commission, Petitioner is to bear if such loss is "properly" allocable to such operations. The Commission in determining such loss acted contrary to the condition imposed upon Petitioner in said previous order. Further, in respect thereto, the Commission acted contrary to all the evidence of record and contrary to all the substantial evidence of record.

c. In disallowing $456,665 in 1952 Federal income tax allowance because of an alleged loss in hydrocarbon or gasoline extraction operations which pursuant to a condition in a previous order of the Commission was not to be considered [fol. 7] as a part of the cost of service applicable to sales by Petitioner in interstate commerce for resale. The action of the Commission in this respect constitutes a departure from all of its previous determinations as to Federal income tax allowance and has the effect of reducing the purported rate of return of 5.75%, which the Commission found to be properly the return to be allowed to Petitioner, to 5.01%.

3. The Commission erred in reducing by $431,061 the amount allowed for rate of return and in allowing Petitioner a rate of return of only 5.75% on the net investment in Petitioner's properties devoted to public service. This amount represents only the historical cost of capital of the investments made in years past, an amount unwarranted by the evidence presented. No adequate notice was given of this method of computation during the proceeding. The rate of return allowed also violates applicable judicial standards since no provision is made for the attraction of capital to the enterprise and amounts, therefore, to confiscation of Petitioner's property contrary to the Fifth Amendment to the Constitution.

4. In making its allocation of costs between sales subject to the Commission's jurisdiction and those not subject to its

jurisdiction, the Commission erred in using as a basis or factor for the spreading of the fixed or demand costs a ratio of volumes of sales which by the Commission's own action as set forth in the record in this case is impossible of accomplishment and in and of itself has the effect of attributing to the nonjurisdictional sales over $200,000 of demand costs which cannot be incurred by such class of sales because of the Commission's own action. Thus, the Commission has acted in an arbitrary, capricious and confiscatory manner and contrary to all of the evidence of record.

5. The Commission erred in prescribing the rates which Petitioner should observe by not making findings or conclusions upon which such rates could be based. Specifically, the means for determining the rates could not be ascertained without an allocation of the cost of service in detail by classes of customers conforming to the rate schedule designations indicated in the Commission's prescribed rates and the revenues determined by the application of the rates set forth in the order of which review is sought hereby by [fol. 8] classes of customers conforming to such rate schedule designations showing volumes, billing demand and the calculation of revenues. The Commission's order, therefore, lacks essential findings upon which the propriety of its rate order may be tested and without which it is impossible to determine whether or not the Commission is prescribing for the future discriminatory and unlawful rates as between classes of customers.

6. The Commission erred in using a cost formula basis for determining what Petitioner is entitled to for its activities in respect of the production of natural gas in the West Panhandle Field of Texas in that the result of such cost formula basis is to give a net wellmouth cost allocable to gas of 1.53¢ per M.c.f. In allocating costs of the hydrocarbon or natural gasoline operations, the Commission used a 5¢ wellhead value of such gas and did likewise in determining the value of gas for percentage depletion purposes in calculating Federal income taxes. The action of the Commission in not using at least such value for determining the justness of Petitioner's rates is arbitrary, capricious, confiscatory and produces an unjust end result.

Wherefore, Colorado Interstate Gas Company, Petitioner, prays:

1. That a copy of this petition forthwith be served upon a member of the Federal Power Commission pursuant to Section 19(b) of the Natural Gas Act (15 U. S. C. §717(b)).

2. That Respondent, Federal Power Commission, be required, in conformity with said Act, to certify and file with the Court the record upon which the order now sought to be reviewed was purportedly entered along with Petitioner's Petition for Rehearing, Vacation and Modification and Motion for Stay of the Commission's Order.

3. That the Court review the order of the Federal Power Commission issued August 8, 1952, the findings and conclusions of the Commission included therein and upon such review reverse, vacate, set aside and hold said order for naught.

[fol. 9] 4. That this Court grant to Petitioner such other and further relief in the premises as the rights and equities of the cause may require.

Respectfully submitted, Colorado Interstate Gas Company, By James Lawrence White, Its Attorney.

[Exhibit D, opinion and order on application for rehearing, is printed at page 188.]

[fol. 10] Before the Federal Power Commission

In the Matters of Canadian River Gas Company and Colorado Interstate Gas Company. Docket No. G-1115.

Pages 1 to 4086 of the certified typewritten record consisting of testimony, oral argument, exhibits, and items by reference, are printed at pages 206 to 592.

Order Instituting Rate Investigation—Issued September

Before Commissioners: Nelson Lee Smith, Chairman; Thomas C. Buchanan, Claude L. Draper, Leland Olds and Harrington Wimberly. September 2, 1948.

It appearing to the Commission that:

(a) Canadian River Gas Company (Canadian River) owns and operates a natural-gas transmission pipeline system extending from the Panhandle gas field in Texas to a point near Clayton, New Mexico, and is engaged in the transportation and sale of natural gas for resale in interstate commerce and is a "natural-gas company" within the meaning of the Natural Gas Act, as amended as heretofore found by the Commission in its order of March 18, 1942, in Docket Nos. G-118, G-121 and G-124 (3 FPC 66-68);

(b) Colorado Interstate Gas Company (Colorado Interstate) owns and operates a natural-gas transmission pipeline system extending from a point near Clayton, New Mexico, to Denver, Colorado. Colorado Interstate purchases natural gas from Canadian River at said point of commencement of its main pipeline and also at a point near [fol. 11] Gray, Oklahoma, purchases additional natural gas from producers in the Kansas-Hugoton field, and transports and sells said natural gas for resale in interstate commerce, and is therefore a "natural-gas company" within the meaning of the Natural Gas Act, as amended, as heretofore found by the Commission in its order of March 18, 1942, in Docket Nos. G-118, G-121 and G-124 (3 FPC 69-71);

(c) On the basis of data available to the Commission, the rates, charges, services or classifications for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission by Canadian River and Colorado Interstate may be unjust, unreasonable, unduly discriminatory or preferential.

The Commission finds that:

It is necessary and proper in the public interest, and to aid in the enforcement of the provisions of the Natural Gas Act, that an investigation be instituted by the Commission into and concerning any rate, charge, service or classification, demanded, observed, charged or collected by Canadian River Gas Company and Colorado Interstate Gas Company, for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and any rule, regulation, practice, or contract affecting such rate, charge, service or classification.

The Commission, on its own motion, orders that:

An investigation be and it hereby is instituted for the purpose of enabling the Commission:

(A) To determine whether any rate, charge, service, or classification demanded, observed, charged or collected by Canadian River Gas Company and Colorado Interstate Gas Company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission or any rule, regulation, practice or contract affecting such rate, charge, service, or classification, is unjust, unreasonable, unduly discriminatory or preferential;

[fols. 12-19] (B) If, after hearing, it shall find that any such rates, charges, services, classifications, rules, regulations, practices or contracts are unjust, unreasonable, unduly discriminatory or preferential, to determine and fix by appropriate order or orders, just, reasonable, non-discriminatory or non-preferential rates, charges, services, classifications, rules, regulations, practices or contracts to be thereafter observed and in force.

By the Commission.

J. H. Gutride, Acting Secretary.

[fol. 20] Before the Federal Power Commission

Extract from a Meeting of the Federal Power Commission Held October 1, 1951

The Commission considered the appeal of staff counsel, at the hearing in the matter of Colorado Interstate Gas Company and Canadian River Gas Company, Docket No. G-1115, on October 1, 1951, from the ruling of the Presiding Examiner that the staff had the burden of proof and of going forward with the testimony, and sustained the ruling of the Presiding Examiner.

Leon M. Fuquay, Secretary.

BEFORE THE FEDERAL POWER COMMISSION

MOTION FOR FINDING THAT STAFF HAS FAILED TO MEET THE BURDEN OF PROOF AND FOR ORDER CLOSING THE DOCKET—Filed November

To the Honorable Emery J. Woodall, Presiding Examiner:

Comes now Colorado Interstate Gas Company and Cana-[fol. 21] dian River Gas Company, by their counsel, and hereby request the Presiding Examiner to certify forthwith to the Commission, pursuant to Section 1.12(d) of the Commission's Rules of Practice and Procedure, the following motion:

Motion is hereby made, in the nature of a demurrer to the evidence, for a finding that the Staff of the Commission has failed to produce evidence at the hearings in this docket held on October 1, 2 and 3, 1951, which would indicate or establish a prima facie case that the rates or charges collected by Colorado Interstate Gas Company (Colorado) and Canadian River Gas Company (Canadian) are unlawful, unreasonable, unjust, discriminatory or otherwise contravene the provisions of the Natural Gas Act (15 U.S.C. § 717 et seq.); and for an order closing the above docket.

Grounds Relied Upon

In view of the fact that the Staff has rested its case and no more evidence in support of a contention that said rates and charges are unlawful can now be made, it is proper for the Examiner and the Commission to consider the question of law as to whether or not, assuming all the facts asserted by the Staff to be true, a valid order of the Commission could issue holding the rates of Colorado and Canadian to be unlawful in any respect.

The rates and charges of both companies which are under investigation in this docket were those previously set by this Commission and incorporated in the FPC Gas Tariff Original Volume No. 1 of Canadian (Item D) and the FPC Gas Tariff Original Volumes 1 and 2 of Colorado (Item E). In view of this fact the previous action of the Commission was legislative in nature and now to attack the rates and charges

it is necessary to bear in mind that any action of the Commission setting rates other than those presently charged would have to be legislative in nature. There can be no dispute that under the provisions of the Natural Gas Act this Commission has authority *only* to fix rates for the future (Federal Power Commission v. Hope Natural Gas Company, 320 U. S. 591, 618), and its findings must be supported by substantial evidence (Natural Gas Act, § 19(b), 15 U.S.C. § 717r(b)). It is submitted that there is no sub-
[fol. 22] stantial evidence in this record which would indicate that for the future the rates and charges of Canadian and Colorado are unlawful. This is so because the Staff's case is bottomed completely upon investment and other book figures of both companies as of June 30, 1951, and utterly fails to take into consideration any adjustments to the chosen period because of added investment already authorized and made. As a matter of fact, the Staff utterly ignored all the facts of the merger of Colorado and Canadian as dealt with the Docket No. G-1326 except for the use of a depletion allowance inapplicable to their period and for a purported loss on gasoline operations (Exhibit 1). Both of these items which were considered by the Commission Staff were ones which serve to reduce the cost of service and thus to inflate alleged excess revenues based upon a test period otherwise using book figures for the year ending June 30, 1951. As Staff Counsel put it:

We have not included the new facilities, and we are perfectly willing to let the Commission determine rates which we say as a matter of law the Commission can determine for the future without including these new facilities. I think that is simple enough." (Tr. p. 278.)

We submit to the Examiner and to the Commission that at this posture of the case there is nothing in the record to indicate the cost of rendering the service to the customers of Canadian and Colorado in the future. It becomes obvious that the failure of the Staff to reflect back into its test year period the elements of the cost of service which are pertinent in the immediate future or to select a test period which would include such elements of cost amounts to an utter failure of its case. This Commission, it is submitted,

cannot lawfully legislate new rates by adopting an order for a future period without finding and grounding those rates upon the cost of all the useful property and other cost elements that the Company will then have in service or will incur. The Commission certainly must have had this very fact in mind when it adopted its opinion in Docket No. G-1326, for there is stated:

[fol. 23] "Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investigation should be brought to a speedy conclusion. In our order issued March 1, 1951, we required Colorado, within four months of that date, to report to us the completion of the acquisition, the commencement of operation by it of facilities acquired, and proof of dissolution of Canadian. Therefore, we have, by order entered today, fixed the date of hearing in the rate case for August 1, 1951, which is one month after the required date for such report."

It is submitted that Colorado and Canadian can make this motion without prejudice to their rights to offer evidence in the event this motion is not granted. Analogy is hereby drawn to Rule 41(b) of the Rules of Civil Procedure for the District Courts of the United States. It is appropriate on this basis for the Commission forthwith to determine the issue posed by this motion and to grant the same immediately so that further expense will not be incurred.

Counsel for Colorado and Canadian are filing this motion only after a deliberate study of the record in this case. It is not filed for any purpose of delay but only for the expeditious determination of a needless controversy. To summarize the whole issue presented hereby, it need only be stated that the Commission Staff has closed its eyes to that used and useful property and to other elements of the cost of service which must be pertinent to this rate inquiry.

Wherefore it is requested that the motion herein made be granted.

Respectfully submitted, Colorado Interstate Gas Company, by James Lawrence White, Counsel. Canadian River Gas Company, by Charles E. McGee, Counsel.

[fol. 24] BEFORE THE FEDERAL POWER COMMISSION

MOTION FOR FINDING THAT STAFF HAS FAILED TO SHOW A CASE, FOR ORDER CLOSING DOCKET AND FOR ORAL ARGUMENT BEFORE COMMISSION EN BANC—Filed November 15, 1951

To The Honorable Emery J. Woodall, Presiding Examiner:

Comes now, Colorado Interstate Gas Company and Canadian River Gas Company, by their counsel, and hereby request the Presiding Examiner to certify forthwith to the Commission, pursuant to Section 1.12(d) of the Commission's Rules of Practice and Procedure, the following motion. Colorado Interstate Gas Company and Canadian River Gas Company hereby move for the following final determinations upon this record:

1. For a finding that the Staff of the Commission has failed to show any purported facts supported by reliable, probative and substantial evidence indicating that the *movents'* rates to be charged for the future are in anywise in violation of the Natural Gas Act;

2. For a finding that the Staff, contrary to law, specifically the Administrative Procedure Act, has failed to notify movants of either the terms or substance of its proposed rate or to describe the actual subjects and issues involved; and

3. For an order closing this docket for either or both of the grounds set forth in "1" and "2" above.

Grounds Relied Upon.

I.

The Staff's Failure to Make a Case.

[fol. 25] The Commission under the Natural Gas Act Section 19(b) (15 U.S.C. 717r(b)) must act upon substantial evidence which by virtue of Section 7 (c) of the Administrative Procedure Act must also be reliable and of probative value. If all the alleged facts supported by evidence

of this character submitted on behalf of the staff are taken to be true, as it should be for the purposes of this motion, the Commission still does not have available to it such material as would enable it to make valid findings and premise a valid rate order.

A. Requirements for a Valid Rate Order.

The Commission has heretofore fixed the presently effective rates of both companies and any rate order now to be entered can only be prospective in effect (Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591, 618). Since only the future rates can be the issue here, the prime question immediately is whether the Staff has shown that the rate structure violates the terms of the Natural Gas Act. We submit that the implements for a decision on this question are missing. Assume for the purposes of this part of the motion that there is a proper rate base determination, proper adjusted revenues and expenses, and proper rate of return, it is obvious that these mean nothing unless they are reduced to an appropriate cost of service and the component costs are spread or allocated to the jurisdictional and the non-jurisdictional business. At the further hearings in this proceeding held on November 6 and 8, 1951, this was not done although the Staff was permitted to reopen and present in effect another direct case (Tr. 289) apparently to overcome some of the objections raised by the movants in their prior motion.

B. There is no Allocation of Costs.

The Commission from the previous rate case involving these companies to the present has determined that the proper allocation basis for rate making purposes is an allocation of costs. This approach has been sustained by the highest authority. We do not understand that the Commission intends to change this approach in this case. The [fol. 26] Staff, however, has not introduced any allocation of costs except for the original test period for the year July 1, 1950, through June 30, 1951 (Exhibit 10), a period which, from the record as a whole, it now appears the Staff

has abandoned (Tr. 328-332).* We now have what is designated as an "allocation of excess earnings" (Exhibit 18). What Mr. French has done is to take from Exhibit 13 certain purported excess revenues (Tr. 320-321) for 1951, 1952 and 1953. These so-called excess revenues were then spread among classes of customers on the same basis he used in Exhibit 10 for spreading costs (Tr. 320). He freely admitted that he made no allocation of costs (Tr. 320). Therefore, Mr. French has assumed or would have this Commission assume that every item in the cost of service will be precisely proportional to every comparable item in his Exhibit 10 which related to the year ending June 30, 1951. Neither the witness French nor any witness has shown that this would be the case. It defies all common sense that such would be the case. No finding of this Commission could be based upon such a non-existent foundation.

It is interesting to note that the so-called excess revenues shown in Exhibit 13, which were the basic figures (the Staff, however, calculated its own income tax, working capital and assumed loss of gasoline operations (Tr. 295-299)), used by Mr. French in his novel Exhibit 18, were in turn based upon estimated figures provided by the companies in a certificate application filed April 24, 1951 in Docket No. G-1677. However, such estimated figures are criticized by the Staff as not being comparable to either the Staff's estimated figures, the figures prepared in an earlier certificate proceeding (Docket No. G-1326), or certain actual figures of the companies for a period ending five months subsequent to the filing in April, 1951 of the G-1677 application (Exhs. 14, 15, 16, Tr. 301-315). Nevertheless, the witness French used the so-called excess revenues of Exhibit 13 as the basis for Exhibit 18.

[fol. 27] To analyze this approach further and really to sum it up, there is here no method for determining whether

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* Although we have referred only to certain pages of the transcript in connection with this motion, an examination of the 59 pages of the transcript of hearing of November 8, 1951, as well as Exhibits 13 through 18, will provide positive proof of our assertion that the record provides no basis for a rate order.

these excess revenues will be allocable in the future to the regulable business. The entire excess can as well be applicable to the direct rates—and the resale gas may even show a deficiency.

The study contained in Exhibit 18 is subject to the very same condemnation which this Commission once leveled at movants: "Nowhere in the entire evidence submitted . . . is there a complete presentation of the entire operations of the company broken down between jurisdictional and non-jurisdictional operations" (3 F.P.C. 32 at 62). Oddly, Exhibit 10 required 13 tables to data comprising 32 pages (exclusive of descriptive narration) to make up an allocation of cost of service study. Aside from the straight commodity allocation all other data was required to support the so-called "commodity-demand" method recommended by Mr. French (Tr. 182). There is no background data or working papers for the single page Exhibit 18 (Tr. 320).

C. No Rate Can Be Constructed from Staff Evidence.

If the revised cost of service exhibit (Exhibit 13) and the so-called allocation exhibit (Exhibit 18) are to be treated seriously, no two-part rate (i. e., with a demand component and a commodity component) can possibly be constructed. The movant Colorado Interstate Gas Company has such a rate (Item E). The Staff in its first direct case constructed such a rate for the merged company (Exhibit 12) based upon the allocated cost of service shown in French Exhibit 10 (Tr. 215-216). Significantly, no rate designed by the Staff has been submitted in this second shot at a direct case. The reason, of course, is apparent—no such rate can be devised under the method used by Mr. French in Exhibit 18.

D. The Staff's Position Is Now the Same as When It Closed Its First Direct Case.

Looking at this record as a whole and realizing that no [fol. 28] allocation of the cost of service has been made in this second chance to meet its burden of proof, it is evident that if the case is to be sustained it must be on the basis of its previous status, namely, the full performance

of the function of showing all rate determinants in per book as of the year ending June 30, 1951. That case, however, is fatally deficient as a matter of law. This is so because the Staff's case is bottomed completely upon investment and other book figures of both companies as of June 30, 1951, and utterly fails to take into consideration any adjustments to the chosen period because of added investment already authorized and made. As a matter of fact, the Staff utterly ignored all the facts of the merger of Colorado and Canadian as dealt with in Docket No. G-1326 except for the use of a depletion allowance inapplicable to their period and for a purported loss on gasoline operations (Exhibit 1). Both of these items which were considered by the Commission Staff were ones which serve to reduce the cost of service and thus to inflate alleged excess revenues based upon a test period otherwise using book figures for the year ending June 30, 1951. As Staff Counsel put it:

"We have not included the new facilities, and we are perfectly willing to let the Commission determine rates which we say as a matter of law the Commission can determine for the future without including these new facilities. I think that is simple enough." (Tr. 278.)

In an attempt to perform the impossible task of rationalizing the evidence presented by the Staff, the Examiner and company counsel inquired if the Staff's test year as shown in the first direct case was abandoned (Tr. 327-328; 331). In answer to this inquiry, Staff counsel stated: "Well, our answer is we are not standing on anything, except all the evidence that has gone in" (Tr. 331). The Examiner pursued the subject and asked what relationship there was between Exhibits 13 through 18 and those presented at the first direct case (Tr. 329). Staff counsel stated that the question could be answered two ways and that, therefore, "* * * we are not going to recommend anything" (Tr. 330). Where all this leaves us we do not know.

[fol. 29]

II.

Lack of Due Process of Law.

The Administrative Procedure Act, which was remedial legislation of the most organic nature, requires "either the

terms or substance of the proposed rule (which by definition 2(c) relates to rates for the future) or a description of the subjects and issues involved" (Administrative Procedure Act 4(a)(3)). Certainly in the present posture of the case no rate is proposed nor, in view of this statement by Staff counsel that:

"Our position as to the use of this material is as follows, Mr. Examiner. You can do it either way Your Honor suggested, use this new material to adjust the figures for the actual, (the first direct case) or you can do the reverse, you can use this new material and adjust that by the actual, and frankly we have not made up our minds which is the approach. Obviously, it is either one of the two, and we are not in a position to say which is the method that should be followed." (Tr. 330.)

is there any notice of anything. There certainly has not been disclosed to anyone what the test period is. Is it the year ending June 30, 1951 (Exhibits 1-12), or any, or all, or an average of 1951, 1952, 1953 (Exhibits 13 and 18)?

In effect the Staff has tried to mend their obviously defective case but analysis will disclose that it is now more procedurally and substantively defective than it was before. To the lack of basis for fixing future rates there now has been added the additional defect of lack of reasonable notice.

III.

The movants, in filing this motion, do so only after a careful and deliberate study of the "evidence" submitted in the Staff's two cases and is presented in order to expedite a determination of an apparently needless controversy and to save all parties further unnecessary expense.

We are of the view that it would be in the public interest [fol. 30] to grant the within motion. It is obvious that by reason of the fact that there has been no experience factor with respect to the companies as merged and because of changing economic conditions, it is difficult to fairly and reasonably present a Section 5(a) rate case at this time. We have heretofore on various occasions represented to the Commission that when Colorado Interstate Gas Company and Canadian River Gas Company are actually merged

and needed property installed and operated that there might be some slight excess revenues on the basis of established precedent. We again repeat that statement.

Frankly, the Staff is faced with a rather difficult situation and we believe that the only proper thing to do is to close this docket and review the merged company's operations a year or so hence.

Wherefore, movants pray that this Commission forthwith grant the motion hereinabove made or fix a hearing before the Commission sitting en banc for the purpose of hearing oral arguments on the issues presented, and for such other and further relief as may be just and proper.

Respectfully submitted, Colorado Interstate Gas Company, By James Lawrence White, Its Counsel. Canadian River Gas Company, By Charles E. McGee, Its Counsel.

BEFORE THE FEDERAL POWER COMMISSION

NOTICE OF CONTINUANCE OF HEARING—November 21, 1951

[fol. 31] Because of the pendency before the Commission of a motion filed by the above-named companies, and the unlikelihood that determination on that matter can be had before November 27, 1951, the date fixed for hearing, notice is hereby given that this hearing is continued from November 27, 1951, to a date to be fixed by further order of the Commission.

Emery J. Woodall, Presiding Examiner.

BEFORE THE FEDERAL POWER COMMISSION

ORDER RECONVENING HEARING—November 30, 1951

On November 15, 1951, Colorado Interstate Gas Company and Canadian River Gas Company (hereinafter referred to as the companies) filed a motion for a finding that Staff has failed to show a case and requested oral argument before the Commission on said motion.

On November 26, 1951, Staff Counsel filed an answer to said motion of the companies.

The companies have reserved the right to cross-examine Staff's witnesses and to offer their own testimony.

The Commission finds:

(1) A majority of the Commission not voting in favor of the request for oral argument on the motion, it is not granted.

(2) It would be in the public interest to conclude the hearings in this matter with all reasonable dispatch.

The Commission orders:

(A) Decision on the motion filed by the companies on November 15, 1951, be and the same is hereby reserved.

(B) The public hearing in this proceeding reconvene to commence on December 10, 1951, at 10:00 A.M. (EST), in the Hearing Room of the Federal Power Commission, 1800 Pennsylvania Avenue, N. W., Washington, D. C.

(C) At said hearing, the companies shall be prepared to proceed with the cross-examination of Staff's witnesses and the presentation of their direct evidence.

[fol. 32] (D) Interested State Commissions may participate as provided by Sections 1.8 and 1.37(f) [18 CFR 1.8 and 1.37(f)] of the Commission's Rules of Practice and Procedure.

By the Commission.

Leon M. Fuquay, Secretary.

BEFORE THE FEDERAL POWER COMMISSION

MOTION TO CONTINUE HEARING.—Filed February 1, 1952

Staff Counsel moves that the hearing in the above-docketed proceeding be continued from February 6, 1952, the date heretofore fixed by the Presiding Examiner to February 18, 1952.

As reason for said continuance, Staff Counsel states that Mr. Frank S. French, a Staff witness who has testified in this proceeding and who is to offer rebuttal testimony on be-

half of the Staff, suffered a fractured arm and other personal injuries as the result of an accident in December 1951; that said Mr. Frank S. French has not been able to return to his duties since the accident; that up until the filing of this motion it was reasonably believed that Mr. Frank S. French would be sufficiently well to return to his duties and testify in this proceeding on February 6, 1952; that it now appears that Mr. Frank S. French will not be able to return to his duties on February 6, 1952; but that it is now expected he will be able to return by February 18, 1952.

Staff Counsel has informed James L. White, Esquire, Counsel for Colorado Interstate Gas Company of the request for said continuance, and counsel offers no objection to Staff Counsel's request.

Jacob Goldberg, Staff Counsel.

[fol. 33] BEFORE THE FEDERAL POWER COMMISSION

NOTICE OF CONTINUANCE OF HEARING.—February 1, 1952

Upon consideration of the Motion of Staff Counsel filed February 1, 1952, notice is hereby given that the hearing in the above-designated matter, now scheduled for February 6, 1952, be and it is hereby continued to February 18, 1952, at 10:00 a.m., in the Commission's Hearing Room, at 1800 Pennsylvania Avenue, N. W., Washington, D. C.

Leon M. Fuquay, Secretary.

BEFORE THE FEDERAL POWER COMMISSION

APPEAL FROM RULING OF PRESIDING EXAMINER—Received February 26, 1952

Staff Counsel appeals from the ruling of the Presiding Examiner granting to Colorado Interstate Gas Company (Colorado Interstate) a recess of the hearings herein for a period of six weeks, from February 20, 1952 to April 8,

1952 (T. 1229). Colorado Interstate requested a continuance of at least eight weeks to prepare for the cross-examination of Staff's rebuttal testimony and such sur-rebuttal as it deems requisite (T. 1218). Staff Counsel objected to such a continuance (T. 1229), and recommended one week as sufficient for Colorado Interstate's purposes.

This proceeding was instituted by Commission order on September 2, 1948. Hearings commenced on October 1, 1951 (postponed from August 1, 1951 at the request of Colorado Interstate), at which time Staff went forward first and presented its cost-of-service study and allied studies based on the actual experience of the Company for the test year ending June 30, 1951. Thereafter, Colorado Interstate was granted a month's recess to prepare for cross-examination [fol. 34] of Staff's witnesses. Four days prior to the reconvening of the hearing, Colorado Interstate filed a motion for a finding that Staff had failed to sustain the burden, on the ground that the test year did not include facilities to be placed in operation in 1952 and at the same time, Colorado Interstate asked for a continuance pending the disposition of the motion. Thereafter, on November 8, 1951, Staff introduced evidence of future operations of the company, based on estimates submitted by Colorado Interstate in an application for a certificate of public convenience and necessity filed by Colorado Interstate at Docket No. G-1677.

After the conclusion of this testimony on November 8, 1951, the hearing examiner continued the hearing to November 27, 1951.* In the meantime, Colorado Interstate filed its second motion for a finding that Staff had failed to sustain the burden, and because of the pendency of this filing the Presiding Examiner continued the matter generally.

By order of November 30, 1951, the Commission reserved ruling on this second motion and found that it was in the public interest that the hearing in this rate proceeding should be concluded with all reasonable dispatch, and ordered Colorado Interstate to be prepared to cross-examine

* This action was taken at the request of Colorado Interstate (T. 335).

Staff's witnesses and to present its own direct testimony on December 10, 1951. A motion filed by Colorado Interstate on December 6, 1951 to continue the hearing beyond December 10, 1951 was denied.

Colorado Interstate cross-examined all of the Staff's witnesses (except for one small phase of Staff Witness Frank French), and introduced its direct case-in-chief. At the request of Staff Counsel, a continuance of seven weeks was granted (the Christmas holidays intervening). Thereafter, Staff requested an additional 12 days because Staff Witness French had become incapacitated due to an accident.

On February 18, 1952, Staff concluded cross-examination of Colorado Interstate's witnesses and offered its rebuttal [fol. 35] testimony based entirely on the direct testimony introduced by Colorado Interstate. It is on the action of the Presiding Examiner granting Colorado Interstate a six weeks continuance following this stage of the proceeding from which this appeal is taken.

The history of these proceedings shows that any further delay in the rendering of a final decision is contrary to the public interest. The Commission noted this fact in its opinion at Docket No. G-1326 approving the merger of Colorado Interstate and Canadian River when it said,

"Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investigation should be brought to a speedy conclusion."

Similarly, the Commission found in its order of November 30, 1951 in this proceeding,

"It would be in the public interest to conclude the hearings in this matter with all reasonable dispatch."

Turning to the background against which the action of the presiding Examiner must be measured, we find that Colorado Interstate has already cross-examined Staff's witnesses on all the evidence presented by Staff save for the rebuttal testimony. In this connection, it may be well to examine the nature and content of Staff's rebuttal testimony. Staff accepted Colorado Interstate's Cost of Serv-

ice study for 1952 (Exhibit 21). It made six adjustments thereto:

(1) Adjusted the rate of return from 6½% to 6%, using the same average net plant balances which the Company used.

(2) Adjusted the depletion allowance for tax purposes using a well head value of 5 cents, rather than the Company's 3.17 cents value, but based on the same volume of gas.

(3) Adjusted the annual depreciation allowance to conform to the service lives recommended by the Staff in its earlier exhibit in this proceeding.

[fol. 36] (4) Adjusted the cost-of-service to reflect the loss on the gasoline operations resulting from the giving up by Colorado Interstate of the gasoline revenues as provided in the merger agreement. The allocation of well mouth and gathering costs to the gasoline was done exactly in the same manner as in Staff's previous exhibit.

(5) Adjusted rate case expense by eliminating two items.

(6) Adjusted the Federal and State Income Tax liability resulting from the five above adjustments.*

Staff cannot conceive that any extended time is necessary to prepare for cross-examination of adjustment (1). It is not a question of rate of return testimony, but merely the mechanics of using one rate of return as against another. The same Staff witness who sponsored Exhibit 26 sponsored the corresponding exhibit (Exhibit 1) for the test year ending June 30, 1951 and was cross-examined on the use of the 6% figure in Exhibit 1.

Concerning adjustment (2) the 5 cents wellhead value was used by the Staff witness in assessing the depletion allowance in Exhibit 1 and he was cross-examined on this point. He has already fully and completely given his reasons for using the 5 cent figure. It was the 5 cent figure sponsored by the company on which the Commission measured the

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* All of Staff's proposed rebuttal exhibits were supplied to the Company at the opening of the session on February 18, 1952, prior to cross examination of the Company's witnesses (T. 939).

benefit of the merger to Colorado Interstate at Docket No. G-1326, and which Colorado Interstate now seeks to repudiate.

As to adjustment (3) (the depreciation allowance), an adjustment to the company's allowance for depreciation was necessary in order to conform to the service lives recommended by the Staff engineer and used in Exhibit 1. The Staff engineer has been cross-examined on his recommended service lives. The Staff engineer did make one addition to his recommendation—the use of a 4 per cent allowance rather than the company's 4.65 per cent on certain of the [fol. 37] new facilities. But no extended time is necessary to prepare for cross-examination of this one point.

As to adjustment (4) (the loss on gasoline operations), the mechanics and method of allocating the well mouth and gathering costs to the gasoline was exactly the same as in Exhibit 1, on which the Staff's witness has been cross-examined. Staff used all the figures and work sheets of Company Exhibit 21, the cost-of-service study introduced by the company. Staff witness has already been cross-examined on the method and reasons for making this allocation. Surely, the task of checking the figures used by Staff witness should not take more than a few days.

In adjustment (5), Staff adjusted the Company's claim for rate case expense by rejecting the fee of $10,000 paid to Mr. D. Houlihan for testifying in Docket No. G-1326, because it is non-recurring item. Further, the Company claimed rate case expense of $210,000 for this proceeding to be amortized over a three-year period. It was admitted by the Company that the figure of $210,000 included possible court review of this proceeding (T. 864). The Staff accountant found from the Company's work sheets that $95,000 was estimated as court review expense. He rejected this amount and recommended that the balance be amortized over 5 years rather than 3 years. This adjustment does not involve any complicated features requiring an extended preparation for cross-examination.

Staff adjustment (6) is the mechanical adjustment to Federal and State Income Taxes necessitated by the previous adjustments. The mathematical method of making adjustments to income tax liability was explained in pre-

vious Staff exhibits. As a matter of fact, the mechanics of the tax adjustments involved here were discussed with the company representatives a month prior to the present hearing (T. 1113). The recomputation of the income tax liability due to the previous adjustments is simply a mechanical detail requiring very little time to check and no new principles are involved here.

Staff Exhibit 27 offered in rebuttal is merely a mathematical breakdown of the average peak-day volume and [fol. 38] revenues, broken down between classes of service, taken from Company's Exhibit 23, and supporting working papers. The figures shown in Staff Exhibit 27 together with Staff's working papers were supplied to the company representatives about a month prior to the hearing (T. 1179).

Staff Exhibit 28 offered in rebuttal by Staff witness French is an allocation study based on Staff's Exhibit 26. Except for different dollar amounts necessarily resulting from a different test year, it is identical in every respect as to method, theory and mechanics with a comparable exhibit (Exhibit 10) for the test year ending June 30, 1951, as to which this witness has been completely cross-examined. This witness stated that Exhibit 28 could be worked out by anyone using the basic figures of Exhibit 26 and the method employed in Exhibit 10 (T. 1206). Surely no extended time is necessary for the purely mechanical task of checking his figures. *

One further fact should be noted. This is a proceeding instituted under Section 5 of the Natural Gas Act. No bond is filed pending its determination. If a rate reduction is in order, and Staff's evidence indicates that the excess of jurisdictional revenues is between 2 and 3 million dollars, every day's delay means that the consumer pays excess revenues without possible redress. The consumer is also

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* Witness Goubleman for the Staff offered two statistical charts to rebut two statements of Company witness Merill. These charts are one page each, representing figures taken from recognized financial publications. As a matter of fact, the company waived cross-examination of Goubleman's prior direct testimony.

entitled to his measure of due process, including a prompt disposition of this proceeding.

It appears that the Presiding Examiner was guided by the length of time required by the Staff to prepare for cross-examination and to prepare its rebuttal testimony (T. 1224). Aside from the fact that the Christmas holidays intervened and the time necessary for the Staff to travel to and from Colorado Springs, Colorado, the Staff first had to analyze and review the company's exhibits and work papers before reaching the determination to accept them, subject to the ad- [fol. 39] justments, and then work out the adjustments. But no such problem is before the company now because it has only to check the six Staff adjustments. The time required by the Staff is no measure of the time required by the company because the issues are much narrower now.

In conclusion then, it is submitted that considering the length of time this proceeding has been pending, and the nature of Staff's rebuttal evidence which was of very limited and narrow scope, the ruling of the Presiding Examiner should be reversed and the hearing reconvened not later than March 4, 1952 for the conclusion of the hearings herein.

Respectfully submitted, Jacob Goldberg, Staff Counsel.

BEFORE THE FEDERAL POWER COMMISSION

ANSWER TO STAFF APPEAL FROM RULING OF PRESIDING EXAMINER.—Received February 29, 1952

Colorado Interstate Gas Company ("Colorado") makes answer to the appeal filed in the above matter as follows:

1. The statements and grounds for such appeal are misleading half-truths as appears from the following:

(a) Staff Counsel neglects to show that on his own motion the proceedings were delayed on November 6, 1951 to put in additional evidence which the Staff could have produced on October 1, 1951, the day hearings commenced.

(b) Staff Counsel speaks of evidence produced by the Staff on February 19 and 20, 1952 as "rebuttal," whereas in

fact, the record clearly indicates that under the guise of "rebuttal" the Staff is seeking to put in still another substantive case-in-chief. This is quite obvious from the fact that Staff Counsel and Staff witnesses contend that the latest exhibits could be used by the Commission, along with all [fol. 40] other evidence in the case, to set rates. Therefore, the evidence is not in answer of or rebuttal to Colorado's cost of service evidence as Staff Counsel would have the Commission believe (Tr. pp. 1085, 1086, 1093, 1143-1145, 1180-1187, 1205-1206).

(c) It is indicated in the appeal that Colorado would have to prepare cross-examination only upon certain simple adjustments. What the appeal does not indicate is that in Exhibit 26, an accounting witness for the Staff has reclassified in six schedules a total of $17,916,022 of costs differently from Colorado. This breakdown of costs on a functional basis must be examined in great detail since it is a Staff endeavor and Colorado cannot risk its propriety or accuracy. Examination of the Staff exhibits will show further detail requiring thorough examination of these exhibits and work papers.

(d) Staff Counsel neglects to state that there is an allocation of costs (Exh. 28) introduced ostensibly as "rebuttal" evidence even though no such allocation study made up a part of Colorado's case-in-chief. What is more important is the fact that the Staff for the first time is seeking to spread demand costs in its fifth recommended allocation study (there is one in Exh. 10, three in Exh. 18 and one in Exh. 28) on a so-called "normal peak day" which is not a day of actual experience. Grave questions arise here and must be thoroughly tested by the process of adequately prepared cross-examination and proper countervailing evidence.

(e) The Staff would have this Commission believe that Mr. French's disability was the only reason for the two full months the Staff had for preparation. If such was the case, why did the Staff wait until the day hearings resumed on February 18, 1952 to serve its so-called rebuttal exhibits on Colorado? If the Staff, in good faith, desires expedition, these exhibits should have been served on Colorado well in advance of February 18, 1952.

(f) The Staff (both Counsel and witnesses) have refused to tell which of the five bases of fixing rates in this record they are advocating. Instead they indicate that the hodge-[fol. 41] podge of five periods can be used separately or together. Since any one of five methods plus the hodge-podge thereof can be used according to the Staff, Colorado now has, in effect, six cases against it which it must answer.

(g) Staff Counsel indicates that Staff witnesses already have been cross-examined on the principles involved. Even if Staff Counsel believed this to be so, Colorado cannot be denied, on his say-so alone, of the opportunity to see whether this is so or not. Even if this were so, and Colorado denies that it is, the Staff is dealing with many millions of dollars which have been reclassified, adjusted and allocated. Drastic things had to be done in great detail to raise an indicated excess over-all revenue from $46,510 (Colorado's Exh. 21) to $3,296,026 (Staff Exh. 26).

(h) Staff Counsel neglects to point out that Colorado was willing to conduct cross-examination beginning on March 17, 1952 but after objection of Staff Counsel to this earlier date and because of the necessity of Staff and Company men traveling it was felt that it would be more economical to have cross-examination and further evidence from Colorado at one group of hearing days, and in furtherance of this plan Colorado proposed to start one day earlier than that set so as to save possibly holding witnesses over a weekend (Tr. pp. 1224-1225, 1228-1229). Staff Counsel was apparently willing to have April 2, 1952 set as a reconvening date (Tr. p. 1227) but this conflicted with an engagement of Counsel in the United States Court of Appeals and, therefore, April 8, 1952 was set (Tr. p. 1227).

2. Staff Counsel would have this Commission believe that Colorado is seeking to delay this rate case. Examination of the record will show that the Staff, rather than Colorado, is responsible. The Staff has set the pace and, after three years in which to prepare, but in its case in October, 1951. Whatever the reason, the Staff found it necessary to put in a new or cumulative case involving three possible test periods in November, 1951. On February 19 and 20, 1952 it put in still another case. If the Staff would originally or [fol. 42] even after the second attempt have had a case

upon which it was willing to rely, these hearings would be over.

3. The time granted is the shortest reasonable time, consistent with due process of law, that the Examiner could set under the circumstances (Tr. pp. 1227-1229). He was the judge of the facts involved on that question. To analyze the matter for the Commission, the Examiner held: "It is my definite conclusion that any time short of April 2 would not be reasonably adequate." (Tr. p. 1227.) It was then pointed out that Counsel had a conflicting engagement in the United States Court of Appeals in New Orleans arising because of a motion of the Commission's Associate General Counsel. April 8, 1952 was then determined by the Examiner.

Examination of the record will show that Colorado requested eight weeks to prepare for cross-examination and the introduction of further evidence. It did not get this amount of time. The record will further disclose that the Examiner fairly inquired into the question and reached what he felt was a fair result. Counsel for Colorado will not quarrel with the result even though, to it, the time does seem too short—considerably shorter than that allowed to the Staff to have men devoted solely to this case examine briefer, less involved documents.

4. The appeal of Staff Counsel was received by Counsel for Colorado one week after the last hearings were recessed and only six days before the date of resumption suggested by Staff Counsel in its said appeal. No prior notice was given of such appeal and its timing is an obvious attempt to embarrass and further harass Colorado. The appeal entirely ignores §1.13 and §1.27(b) (7) of the Commission's Practice Rules and The Administrative Procedure Act, §7 wherein it is clear that the Examiner may control the question raised by this appeal. It would appear that Staff Counsel by his so-called appeal is endeavoring to circumvent the purpose of §1.28 of the Rules of Practice which requires referral by the Examiner. If the device of Staff Counsel is successful, any party can then feel free to appeal [fol. 43] to the Commission on any interlocutory question so long as hearings are in recess. The procedure of Staff Counsel is patently wrong.

5. Not in response to the appeal, but for the Commission's information, Colorado's Counsel are of the opinion that only by long and very hard work can they be ready to proceed with cross-examination and further evidence by April 8, 1952. It would be impossible to proceed before that date.

Wherefore, the appeal filed by Staff Counsel should be dismissed.

Respectfully submitted, James Lawrence White, Charles E. McGee, Counsel for Colorado Interstate Gas Company.

BEFORE THE FEDERAL POWER COMMISSION

ORDER ON APPEAL FROM RULING OF PRESIDING EXAMINER—March 7, 1952

Before Commissioners: Thomas C. Buchanan, Chairman; Claude L. Draper, Nelson Lee Smith and Harrington Wimberly. March 6, 1952.

On February 26, 1952, Staff Counsel filed an appeal from the ruling of the Presiding Examiner granting to Colorado Interstate Gas Company (Colorado Interstate) a recess of the hearings herein from February 20, 1952 to April 8, 1952.

On February 29, 1952, Colorado Interstate filed its Answer to said Appeal of Staff Counsel.

The Commission finds:

On the record in this proceeding, including the matters set forth in the pleadings above mentioned, it would not be in the public interest to recess this hearing for the length of time fixed by the Presiding Examiner.

[fols. 44-56] The Commission orders:

(A) The public hearing in this proceeding shall reconvene, commencing on March 25, 1952, at 10:00 a.m. (EST) in the Hearing Room of the Federal Power Commission, 1800 Pennsylvania Avenue, N. W., Washington, D. C.

(B) Colorado Interstate Gas Company shall be prepared on said date to proceed with cross-examination of Staff rebuttal evidence and the presentation of evidence in response to Staff's rebuttal evidence.

(C) Interested State commissions may participate as provided by Sections 1.8 and 1.37(f) [18 CFR 1.8 and 1.37(f)] of the Commission's Rules of Practice and Procedure.

By the Commission.

Leon M. Fuquay, Secretary.

Date of Issuance: March 7, 1952.

[fol. 57] BEFORE THE FEDERAL POWER COMMISSION

MOTION TO OMIT INTERMEDIATE DECISION PROCEDURE, OR IN THE ALTERNATIVE, FOR ISSUANCE OF TENTATIVE DECISION.—Filed April 9, 1952

Pursuant to Section 1.30(c) of the Commission's Rules of Practice and Procedure, Staff Counsel moves and requests that the intermediate decision procedure be omitted in this proceeding. In the alternative, Staff Counsel requests, pursuant to Section 1.30(b) of said Rules of Practice and Procedure, that the Commission issue a tentative decision herein.

[fol. 58] As reasons for the motion, Staff Counsel states the following: This is a rate proceeding initiated pursuant to Section 5 of the Natural Gas Act by the Commission on its own motion by order of September 2, 1948. The order instituting this rate investigation recited that it appeared "[O]n the basis of data available to the Commission the rates * * * [of] Colorado Interstate may be unjust, unreasonable, unduly discriminatory or preferential."

Hearings in this proceeding did not commence until October 1, 1951, more than three years after the institution of the investigation of Colorado Interstate's rates. There have been six separate hearing sessions in this matter since October 1, 1951, concluding on April 4, 1952.

Staff Counsel respectfully further states that Exhibit 10 introduced by the Staff on October 2, 1951, showed that the

company's operations for the year ending June 30, 1951 resulted in excess revenues on the jurisdictional business of more than $3,000,000. Staff Exhibit 28, based on Colorado Interstate's own estimates of operating expenses and revenues for the calendar year 1952, as adjusted by the Staff, showed excess revenues over a fair return on the jurisdictional business of more than $3,000,000.

Colorado Interstate has been collecting excess revenues for more than three years since the Commission instituted this proceeding. The customers of Colorado Interstate, however, have no redress under a Section 5 proceeding for such past excessive exactions. Their relief can only come when the Commission enters an order reducing rates, and such relief is long overdue. In the circumstances here present, the Commission can with justice make the prerequisite findings required by the Administrative Procedure Act and omit the intermediate decision procedure.

In the alternative, if the Commission does not grant the above request, Staff Counsel requests that the Commission itself issue a tentative decision herein in lieu of the Presiding Examiner's report. Such action may be taken by the Commission, pursuant to Section 1.30(b) of the Rules and [fol. 59] Section 8(a) of the Administrative Procedure Act, without the necessity of making the statutory finding required for the omission of the intermediate decision procedure. The Administrative Procedure Act does not require the Commission to make any findings to support the Commission action in issuing a tentative decision in rate matters. However, it is submitted the foregoing reasons to support the omission of the intermediate decision procedure are sufficient of themselves to warrant the tentative decision procedure here. It should be recalled that unlike a proceeding under Section 4 of the Natural Gas Act, there is no provision in a Section 5 proceeding for the filing of a bond to insure the repayment of excessive revenues collected.

It is in the public interest to put an end to the exaction of excessive revenues by Colorado Interstate. There is every reasonable expectation that the adoption of the tentative decision procedure will conclude this proceeding more promptly than otherwise. The omission of the intermediate decision procedure is warranted by the record in this pro-

ceeding and will provide even more expeditious determination of this matter.

Respectfully submitted, Jacob Goldberg, Staff Counsel.

BEFORE THE FEDERAL POWER COMMISSION

ANSWER TO STAFF COUNSEL'S MOTION TO OMIT INTERMEDIATE DECISION PROCEDURE OR, ALTERNATIVELY, FOR THE ISSUANCE OF TENTATIVE DECISION BY THE COMMISSION.—Filed April 17, 1952

Colorado Interstate Gas Company (Colorado) by its counsel hereby answers the motion of Staff Counsel filed April 9, 1952 for omission of the intermediate decision procedure or, in the alternative, for issuance of a tentative decision by the Commission. In answer to said motion, Colorado states the following:

[fol. 60] 1. This motion cannot be made pursuant to Section 1.30(c) of the Commission's Rules of Practice and Procedure because:

(i) the concurrence of Colorado has not been alleged, nor can it be alleged since Colorado refuses to occur therein;

(ii) there is not specified whether there should be opportunity for presenting oral argument or filing briefs before the Examiner or the Commission; and

(iii) there is not specified whether there is desired an opportunity for presenting proposed findings and conclusions with supporting reasons therefor.

2. The Commission may not omit the intermediate decision procedure either upon motion of Staff Counsel or upon its own motion under the Administrative Procedure Act, Section 8(a) (for the convenience of the Commission, all of Section 8 is attached as an Appendix). Section 8(a) of the Administrative Procedure Act, by virtue of judicial holdings (mainly, Universal Camera Corporation v. N.L.R.B., 340 U.S. 474), and the legislative history of the Administrative Procedure Act clearly does not allow the omission of the intermediate decision procedure where issues are sharply controverted or where the case tends to become accusatory in nature (see portion of the legislative

history quoted under "2" sub). The situation in the instant case clearly is one in which the decision of the presiding officer is not only desirable but absolutely necessary as the following will show:

(i) As the Supreme Court held in Universal Camera Corporation vs. N.L.R.B. (supra), an examiner's decision has an important bearing upon the substantiality of the evidence upon which Commission action must rest. The Supreme Court stated:

"We intend only to recognize that evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion. The findings of the examiner are to be considered along with the [fol. 61] consistency and inherent probability of testimony. The significance of his report, of course, depends largely on the importance of credibility in the particular case. To give it this significance does not seem to us materially more difficult than to heed the other factors which in sum determine whether evidence is 'substantial'." (340 U. S. at 496-497.)

The Supreme Court in the Universal Camera case also noted the provisions of Section 8(b) of the Administrative Procedure Act and held the Examiner's report to be as much a part of the record as the testimony. Similarly, the House Committee is reporting on the Administrative Procedure Act stated in respect of examiner's decisions:

"They become a part of the record and are of consequence, for example, to the extent that *material facts in any case depend on the determination of credibility of witnesses as shown by their demeanor or conduct at the hearing.*" Administrative Procedure Act, Legislative History, 79th Cong. 2d. Sess., Senate Document No. 248, p. 272, emphasis added.)

Examination of the record in this case will show that credibility has got to be one of the paramount factors. Colorado contends that the Staff case is defective and has not been supported by reliable or credible evidence. As the record in this case shows, Staff Counsel and Staff witnesses alike have refused to notify or testify as to what base or

test period they are depending upon or would recommend. The Staff and its Counsel say that any of five test periods (see Exhs. 1, 13 and 26) might be used, or a combination thereof might be appropriate (Tr. pp. 330, 1085, 1086). In the course of the cross-examination of all of Staff witnesses there appeared to be a reluctance to answer and evasiveness to answers given both with respect to the proper test period or periods (Tr. pp. 1143-1145, 1180-1187, 1205-1206) and also with respect to the manner in which the Staff made its own calculations or adjusted estimates presented on behalf of Colorado (Tr. pp. 424-427, 437-442, 447). This was particularly true in the later phases of the case (Tr. pp. 1252, 1254, 1255, 1256-1262). The record disclosed only those evidences of a witness' demeanor which can be re-
[fol. 62] corded in the written progress of the hearing. Counsel for Colorado allege that there were many other instances of where the demeanor of witnesses in this case has an important bearing upon evaluating the worth of their evidence and only the presiding officer is competent to make this necessary determination.

(ii) The record in this case will show that from the beginning the issues have been sharply controverted and the proceeding has been accusatory in nature. The best late evidence of this fact is contained in the motion of Staff Counsel to which this is in answer wherein he states on Page 1 of his motion:

"Colorado Interstate has been collecting excess revenues for more than three years since the Commission instituted this proceeding."

And in the last paragraph of the motion Staff Counsel states:

"It is in the public interest to put an end to the exaction of excessive revenues by Colorado Interstate."

A similar set of accusations appear in the transcript (Tr. pp. 334, 420). It is obvious that Staff Counsel is grounding his motion upon what he hopes will be the end result of a valid Commission determination, i. e. that Colorado's revenues are excessive. The important factor at this juncture of the case, however, is that Staff Counsel makes such ac-

cusations not as his contention but as a final fact and, therefore, expects this Commission to shut its eyes to the evidence introduced on behalf of Colorado which shows instead of an excess of allowable revenue the Company in fact has a deficiency. There can be no doubt that the contention being made on behalf of Colorado is that there is no excess revenues. This in itself requires the most careful consideration of over 40 involved exhibits and the examination of 1,798 pages of testimony. This all brings into focus what was said during the legislative progress of the Administrative Procedure Act:

"The alternative intermediate procedure which an agency [fol. 63] may adopt in rule-making or determining applications for initial licenses is broadly drawn. But even in those cases, if issues of fact are sharply controverted or the case or class of cases tends to become accusatory in nature, sound practice would require the agency to adopt the intermediate recommended decision procedure." (Report of House Judiciary Committee, Administrative Procedure Act, Legislative History, 79th Cong. 2d. Sess., Senate Document No. 248, p. 273.)

3. In view of the foregoing, if the Commission were to omit the intermediate decision procedure in this case on the motion of Staff Counsel, it would be acting contrary to its own rules and requirements; and if the Commission were to decide to omit the intermediate decision procedure upon its own motion the effect would be to deprive Colorado of a part of a record and that scrutiny of the whole record which Colorado is entitled to by the one most competent to judge the overwhelmingly important item of the credibility of the witnesses and the evidence. In effect, under the opinion of the Supreme Court in the Universal Camera case (supra), the Commission would be denying an important factor in the determination of that substantiality of evidence upon which its findings under the Natural Gas Act (§19(b)) must depend.

4. Alternatively, Staff Counsel asks that this Commission issue a tentative decision. Examination of the legislative history of the Administrative Procedure Act (see part quoted under "2" supra) will show conclusively that a

tentative decision by the Commission is no more appropriate in this case than would be the omission of the intermediate decision procedure (see Legislative History of the Administrative Procedure Act, House Report, 79th Cong. 2d. Sess., Senate Document No. 248, pp. 272-273). As a practical matter under the Commission's rules (1.30(b)) it would appear that such tentative decision would only serve further to delay this proceeding since a tentative decision is subject to all the exceptions and subsequent procedures as is the case with an intermediate decision (Commission's Rules of Practice, 1.31). It would be necessary, [fols. 64-65] therefore, for the Commission itself to study this record in order to render an intelligent tentative decision and acquaint itself with material and involved data and to resolve conflicts and spend the necessary time in doing so, whereas the Presiding Examiner has heard the whole case and is in a position to render a decision within the shortest possible time after the briefs provided for have been submitted by the Staff, by Colorado and by intervenors. Even if the Commission were to do all of these things, it would still be denying to Colorado in a sharply controverted and accusatory case its right to the Examiner's appraisal.

5. The fair construction of Section 8 of the Administrative Procedure Act as portrayed in its legislative history and as expounded in the Universal Camera case is that the intermediate procedure through the Examiner is required and denial of the Examiner's decision would be tantamount to disallowing a proper part of the record upon which Commission action must be grounded. To grant in any particular the motion of Staff Counsel would deprive Colorado of the hearing to which it is entitled under Section 5(a) of the Natural Gas Act and by the Constitutional requirement of due process of law.

Wherefore, it is clear that consistent with the rights of Colorado and consistent with the requirement that an intelligent and fair result obtain it would be inappropriate to grant the motion of Staff Counsel to which this response is made and said motion must, therefore, be denied.

Respectfully submitted, James Lawrence White, Charles E. McGee, Counsel for Colorado Interstate Gas Company.

[fol. 66] BEFORE THE FEDERAL POWER COMMISSION

ORDER OMITTING INTERMEDIATE DECISION PROCEDURE AND FIXING DATE FOR ORAL ARGUMENT.—Issued May 26, 1952

Before Commissioners: Thomas C. Buchanan, Chairman; Dale E. Doty, Claude L. Draper, Nelson Lee Smith and Harrington Wimberly. May 23, 1952.

On April 9, 1952, Staff Counsel filed a motion, pursuant to Section 1.30 of the Commission's Rules of Practice and Procedure, that the intermediate decision procedure be omitted in this proceeding, or, in the alternative, the Commission issue a tentative decision.

On April 17, 1952, counsel for Colorado Interstate Gas Company (Colorado Interstate) filed its answer opposing said motion of Staff Counsel.

The record shows that this proceeding was initiated pursuant to the authority of the Natural Gas Act on the Commission's own motion, by order of September 2, 1948, instituting an investigation of the rates of Colorado Interstate[1] for the reason that it appeared to the Commission on "the basis of data available to the Commission, the rates, charges, services or classification or sale of natural gas subject to the jurisdiction of the Commission by Canadian River and Colorado Interstate may be unjust, unreasonable, unduly discriminatory or preferential." Staff studies based on Colorado Interstate's and Canadian River's Annual Reports to the Commission (FPC Form No. 2) showed excess revenues above a fair rate of return of $2,000,000 for the two companies.

Subsequent to the institution of the rate proceeding and after the Staff had completed its studies of the records and operations of Colorado Interstate and Canadian River in [fol. 67] preparation for a hearing, Colorado Interstate and Canadian River filed on February 13, 1950, at Docket No. G-1326, a joint application, as amended, on April 4, 1950, for a certificate of public convenience and necessity

[1] The order of September 2, 1948 included the investigation of the rates of Canadian River Gas Company, which since January 1, 1952, has been merged with Colorado Interstate.

authorizing (1) Colorado Interstate to acquire by merger the properties of Canadian River and to merge Canadian River into Colorado Interstate and (2) to construct and operate certain natural-gas pipe-line facilities. By order of July 20, 1950, the Commission authorized the construction and operation of the natural-gas pipe-line facilities referred to above, but reopened the hearing for purpose of determining certain aspect of the proposed merger. By opinion and order of February 28, 1951, a certificate was issued authorizing the merger.

In the meantime hearing on the instant rate proceeding was deferred pending the disposition of the merger proceedings at Docket No. C-1326. The Commission, therefore, in its opinion of March 16, 1951, authorizing the merger stated (Opinion No. 209, (mimeographed), page 23):

"Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investigation be brought to a speedy conclusion."

Accordingly, by order of March 16, 1951, the Commission fixed August 1, 1951, as the date of hearing in this proceeding.

On July 1, 1951, Colorado Interstate and Canadian River filed a motion to continue the hearing from August 1, 1951, to February 1, 1952. By order of July 25, 1951, the Commission granted Colorado Interstate and Canadian River a continuance of the hearing in this proceeding from August 1, 1951, to October 1, 1951.

Hearing in this matter commenced on October 1, 1951, with Staff's presentation of its evidence. At the conclusion of the Staff's evidence on October 3, 1951, counsel for Colorado Interstate and Canadian River requested and received a continuance until November 6, 1951, to prepare for cross-examination. On November 2, 1951, Colorado Interstate and Canadian River filed (1) a motion for a finding that Staff has failed to meet the burden of proof and (2) a mo- [fol. 68] tion for continuance of the hearings to November 14, 1951. After the Staff had introduced further testimony on November 8, 1951, the Presiding Examiner fixed November 27, 1951, for the reconvening of the hearing to enable

Colorado Interstate and Canadian River to cross-examine the Staff's witnesses and to introduce its own case-in-chief, Colorado Interstate and Canadian River, however, on November 15, 1951, filed a second motion for a finding that the Staff had failed to sustain the burden of proof. By notice dated November 21, 1951, the Presiding Examiner continued the hearing to a date to be fixed by further order of the Commission because of the pendency of the second motion filed by the companies. On November 30, 1951, the Commission reserved decision on the second motion pending conclusion of the hearing and finding that "it would be in the public interest to conclude the hearing in this matter with all reasonable dispatch," ordered the hearing to reconvene on December 10, 1951. On December 6, 1951, Counsel for the companies filed a motion to continue the hearing scheduled for December 10, 1951, to a date to be fixed by further order of the Commission. By notice dated December 6, 1951, this motion for continuance was denied.

Beginning on December 10, 1951, and concluding on December 17, 1951, the companies cross-examined Staff's witnesses and introduced their own case-in-chief. The hearing was then continued to February 1, 1952, extended to February 6, 1952, to enable Staff to cross-examine the companies' witnesses and to introduce its rebuttal. Thereafter, to enable Colorado Interstate to prepare for cross-examination of Staff rebuttal, the hearing was recessed to March 25, 1952, on order on Staff appeal taken from the ruling of the Presiding Examiner. After cross-examination of Staff introduction of further testimony by Colorado Interstate and cross-examination thereof by Staff, the hearing concluded on April 4, 1952.

This proceeding has been in progress for a regrettably long period of time, responsibility for which fact is not attributable to any one particular party. In view of the fact that this Commission has no power of reparation with respect to past rates, which may or may not prove to be excessive, it appears that the record in this proceeding [fols. 69-74] presents the kind of situation requiring the omission of the intermediate decision procedure as provided in the Administrative Procedure Act.

The Commission finds:

Based on the foregoing facts taken together, due and timely execution of its functions imperatively and unavoidably requires the Commission to omit the intermediate decision procedure in this proceeding.

The Commission orders:

(A) The intermediate decision procedure be and the same is hereby omitted in this proceeding, and the Presiding Examiner is hereby directed to certify the record to the Commission.

(B) Main briefs and reply briefs shall be filed on the dates heretofore fixed by the Presiding Examiner.

(C) Oral argument be had before the Commission on June 9, 1952, at 10:00 A. M. (EDST) in the Hearing Room, Federal Power Commission, 1800 Pennsylvania Avenue, N. W., Washington, D. C., concerning the matters and issues involved in this proceeding.

(D) Parties in this proceeding who intend to participate in the oral argument shall so notify the Secretary of the Commission on or before June 2, 1952, and of the time requested for presentation of their argument.

By the Commissioner. Commissioner Doty not participating.

Leon M. Fuquay, Secretary.

* * * * * * *

[fol. 75] Before the Federal Power Commission

Application for Rehearing of Order Issued May 26, 1952 Omitting Intermediate Decision Procedure—Received June 4, 1952

Colorado Interstate Gas Company (Colorado) by its counsel hereby applies for rehearing of the order issued May 26, 1952 by this Commission wherein it was determined to omit the intermediate decision procedure. As grounds for granting said rehearing, Colorado states the following:

1. The effect of said order of the Commission denies to Colorado its right to submit briefs upon the merits and pro-

cedural aspects of this rate controversy since the order was issued on the day that final briefs were due and was received the day after said final briefs were filed. A participant to an adversary proceeding, such as this one has proved to be, prepares briefs and argument to one who has presided at the reception of all evidence and who has been able to study the demeanor and manner of witnesses. As the order of the Commission notes, the application for [fol. 76] omission of the intermediate decision procedure of Staff Counsel was filed April 9, 1952 and was answered on behalf of Colorado on April 17, 1952. There was more than adequate time after the answer was received for the Commission to pass upon the motion, and the action of the Commission in failing to issue its order omitting the intermediate decision procedure until the day final briefs were due effectively thwarted any endeavor to brief the whole question to the Commission rather than to the Presiding Officer.

2. The Commission recites as one of the facts upon which it was determined to omit the intermediate decision that it lacks reparation authority. The denial by Congress of reparation authority to this Commission does not in any way enlarge the jurisdiction of this Commission or in any way confer upon it a right to prejudice parties who are subject to proceedings before it.

3. The Commission by its said order finds that all of the recited facts in said order require the omission of the intermediate decision. Among the facts set forth in the petition was the motion of Staff Counsel to omit the intermediate decision. Under the Rules of this Commission (Section 1.30(c)), the intermediate decision could not be omitted upon the basis of this motion.

4. The Commission may not upon its own motion omit the intermediate decision under Section 7(a) of the Administrative Procedure Act as the same has been construed by Universal Camera Corporation vs. N. L. R. B. (340 U. S. 474) and the legislative history of the Administrative Procedure Act, all as fully set forth in the answer to Staff Counsel's motion to omit the intermediate decision procedure filed by Colorado in this docket.

5. This proceeding has become one obviously accusatory in nature and one in which issues of fact have been sharply controverted, all of which have been fully set forth in Colorado's answer to the motion of Staff Counsel in this matter. Reference to the record in this case will show upon its face [fol. 77] that this is a proceeding peculiar in that it requires the attention and decision of one who has been able to observe the manner and demeanor of witnesses and, therefore, properly arrive at conclusions bearing upon the credibility of testimony and other evidence. Matters of record in respect thereof have been fully set forth in the answer of Colorado to the motion of Staff Counsel above referred to.

7. The net effect of the Commission's action in omitting the intermediate decision procedure in this case is to deny Colorado its right to a fair hearing under applicable Constitutional and statutory safeguards. It is recited by the Commission that there has been delay in the decision of this case but that no party is responsible therefor. It is submitted that no reason appears, nor is there any finding made, to determine the necessity of denying to Colorado a full and fair determination of the issues involved under every Constitutional and statutory safeguard. No matter what the necessities of time are within the Commission's concept thereof, there is never an excuse for failing to adhere to the concept of fair play.

Wherefore, it is submitted to the Commission that it has erred in ordering the omission of the intermediate decision procedure in this case and that a rehearing of its order issued May 26, 1952 should be had and said order vacated forthwith.

Respectfully submitted, By James Lawrence White, By Charles E. McGee, Counsel for Colorado Interstate Gas Company.

* * * * * * *

Before the Federal Power Commission

Opinion, Finding and Order Reducing Rates— Issued August 8, 1952

[fol. 78] Before Commissioners: Thomas C. Buchanan, Chairman; Dale E. Doty and Harrington Wimberly. July 31, 1952.

Opinion No. 235

On September 2, 1948, the Commission instituted an investigation pursuant to Section 5 of the Natural Gas Act, to determine whether any rate, charge, service or classification observed, charged or collected by Canadian River Gas Company (Canadian River) and Colorado Interstate Gas Company (Colorado) for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission is unjust, unreasonable, unduly discriminatory or preferential. Said Section 5 of the Natural Gas Act empowers the Commission to determine the just and reasonable rates to be thereafter observed and in force and to fix the same by order on a finding after hearing that any such rate is unjust, unreasonable, unduly discriminatory or preferential.

Petitions to intervene in the proceeding were filed by Public Service Company of Colorado, Natural Gas Pipeline Company of America, Public Utilities Commission of the State of Colorado, The City of Denver and The City of Colorado Springs, all of which petitions were granted.

Pursuant to our Order of Investigation, an extensive field examination of the books, records, facilities and operations of Respondent[1] was made by our staff. Hearings

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[1] Subsequent to the initiation of this proceeding but prior to the commencement of hearings, the Commission authorized Colorado to acquire by merger the properties of Canadian River. Said merger was consummated on December 31, 1951. Hereafter, therefore, when we refer to Respondent, the reference will include both companies unless the text of the Opinion otherwise indicates.

in this proceeding commenced on October, 1951, and concluded on April 4, 1952. Exhibits numbering 44 were received in evidence and 1,798 pages of testimony were recorded. By order of May 23, 1952, we omitted the intermediate decision procedure in this matter and fixed June 9, 1952, as the date for oral argument before the Commission. The staff of the Commission and the Respondent companies introduced evidence in this proceeding. None of the inter- [fol. 79] venors offered any evidence, filed briefs or took part in the oral argument.

Following the oral argument before the Commission, by letter of June 11, 1952, Counsel for Colorado transmitted:

(1) a copy of the minutes of the meeting of the Board of Directors of Colorado held on March 10, 1952.

(2) a copy of the minutes of the meeting of the Board of Directors of Colorado held on May 16, 1952.

(3) a copy of the Post-Effective Amendment to the Registration Statement filed by Colorado with the Securities and Exchange Commission on April 30, 1952.

In his letter of transmittal, counsel for Colorado requested that these three documents be considered a part of the record in this proceeding. Accordingly, they may be deemed to be incorporated into the record in this proceeding by reference to the official files of the Commission, and they are hereby identified as Item- R, S and T, respectively.

Colorado owns and operates extensive natural gas production, gathering and processing facilities in the West Panhandle field of Texas and also purchases and processes large volumes of natural gas in the Hugoton field of Kansas. Colorado also owns and operates a transmission pipe line system extending from such fields to its terminal market area at Denver, Colorado. Sales are made from such pipe lines to distributing utilities for resale and to industrial customers. Colorado admits that it is a "natural-gas company" under the Act. Respondent's rates have been the subject of another Commission rate proceeding In the Matter of Colorado Interstate Gas Company, 3 F. P. C. 32, Affirmed 324. U. S. 581.

The staff of the Commission presented evidence from which the staff concluded that the rates of Colorado subject to our jurisdiction should be reduced by the sum of $3,227,287. Colorado contends, however, that it is not earning sufficient revenues to yield a fair return on its jurisdictional sales.

We have carefully considered the entire record including the briefs, oral arguments and requested findings. Our find- [fol. 80] ings and conclusions, hereinafter set forth, are dispositive of each and every one of the requested findings. It is our opinion that the presently effective rates and charges of Colorado are unjust, unreasonable and excessive and should be reduced as hereinafter ordered.

The following table summarizes the difference between the staff and Colorado with reference to the rate base, and the various elements which make up the cost of service. We will discuss these differences and thereafter take up the various issues relating to cost allocation and the form of rates.

Rate Base	Staff	Colorado	Difference
Average Balance			
Plant in Service	$73,162,834	$73,162,834	.....
Plant Held for Future Use	269,213	269,213	.....
	$73,432,047	$73,432,047	.....
Less: Average Reserve for Depreciation and Depletion	18,182,793	18,253,259	$ 70,466
Contributions in Aid of Construction	139,302	139,302	.....
Net Investment in Plant	$55,109,952	$55,039,486	$ (70,466)
Working Capital			
Cash Allowance	673,363	779,623	106,260
Material & Supplies	1,381,331	1,381,331	.....
Total Rate Base	$57,164,646	$57,200,440	$ 35,794
Revenues			
Gas Service Revenues	$17,962,532	$17,962,532	.....
Other Gas Revenues	1,141,520	1,141,520	.....
Total Revenues	$19,104,052	$19,104,052	.....
Cost of Service			
Operating Expenses	$ 8,417,707	$ 9,282,680	$ 864,973
[fol. 81]			
Depreciation and Depletion	2,595,427	2,736,361	140,934
Taxes Other than Federal Income	1,835,229	1,898,994	63,765
Federal Income Taxes	.....	2,306,808	2,306,808
Return	3,286,967	3,718,028	431,061
Loss on Gasoline Operations	(585,528)	.....	585,528
Total Cost of Service	$15,549,802	$19,942,871	$4,393,069

Test Period.

There is no dispute as to the test period, both the staff and Colorado using the calendar year 1952. The basic figures presented which was based on the most recent actual past operating experience adjusted to reflect known changes combined on a pro forma basis for the merged corporation including the facilities authorized at Docket G-1326 and G-1677 which went into operation in part in 1951 and the balance in 1952. We are of the opinion and find that the appropriate test period is the calendar year 1952.

Rate Base.

As shown by the above table, the net difference of $35,794 between the staff and Colorado as to the rate base for 1952 relates to the amount deducted for accrued depreciation and depletion and to the cash allowance for working capital. The difference of $70,466 in the average balance for depreciation and depletion flows from the divergent methods used by Colorado and the staff in determining the annual depreciation provision for the year 1952. As will be noted from the Cost of Service section of the foregoing table, such difference in the annual expense for depreciation and depletion amounts to $140,934. The effect upon the average depreciation reserve balance is about one-half of that sum.

The staff made a comprehensive study of the company's facilities, its gas reserves and retirement experience and from such study developed service lives for each particular segment of the company's property. The testimony shows [fol. 82] that major consideration was given to the functional or economic life of the enterprise. Colorado's claimed annual allowance for depreciation was based upon the method which it has followed since January 1, 1948, in accounting for depreciation on its books.[2] Under this

[2] The "remaining service life" method accounts for approximately 85% of the annual provision for depreciation and depletion the remainder being calculated on the unit of production and other bases.

method which it terms the "remaining service life method" the annual provision is determined by taking the average net investment for the year and dividing it by the estimated number of years life remaining of the company's properties. The company estimated the remaining life of its properties to be 25 years from January 1, 1948.

Prior to the adoption of such method on January 1, 1948, and since the conclusion of the earlier rate proceeding In the Matter of Colorado Interstate Gas Co. (3 F. P. C. 32) the Company had also followed the straight line—service life basis of depreciation as determined by the Commission in that case. It presented no evidence which would justify a departure from the straight line-service life basis of depreciation which we determined in the prior rate proceeding and which the staff has used herein. The company's contention appears to be that the service life method is inappropriate as there is no present basis for the projection of its present gas reserves beyond 1972 and refers to a statement in our decision (Re: Colorado Interstate Gas Company, et al., Opinion No. 209, March 20, 1951, Docket No. G-1326) as authority therefor. Colorado has misinterpreted such statement for what we there said related solely to Canadian's acreage in the West Panhandle field and was not an appraisal of the company's overall reserve picture or economic life.

The resulting difference between the staff and the company in the annual depreciation provision for 1952 exclusive of that portion relating to the additional facilities authorized in Docket Nos. G-1326 and G-1677 amounts to [fol. 83] $44,258. As to such additional facilities the difference amounts to $96,676. The staff witness recommended a 25-year service life for these new facilities based upon his appraisal of the reserves of Colorado in the West Panhandle field, the Hugoton field and the additional reserves proposed to be and in fact subsequently acquired by Colorado in the Keyes fields and South Keyes fields in Oklahoma. Under the company's remaining life method, Colorado computed the annual provision for 1952 on a remaining life of 20½ years for the facilities proposed to be placed in service during such year.

From our review of the record we are convinced that the service lives recommended by the staff witness are reasonable and proper under the circumstances and we therefore find that such service lives should be used in computing the annual depreciation provision for 1952.

Colorado argues that a major defect exists with respect to the staff's depreciation studies contending that as no correlation was made between annual and accrued depreciation, which if made, would result in a lesser amount for accrued depreciation thus effecting an increase in the rate base. It seems hardly necessary to point out that the reserve for depreciation could not properly be adjusted for past accrued depreciation relating to the property certificated in Docket Nos. G-1326 and G-1677, since most of such properties did not go into service until 1952. Therefore the alleged lack of correlation could only arise from the small annual difference of $44,258 applicable to Plant other than that authorized in the above dockets.

It has not been the practice to adjust depreciation reserves either upward or downward whenever changing circumstances makes necessary minor revisions of current depreciation rates. We have in some instances, used the reserve requirement when we found that book reserves were accumulated through haphazard, unsound or improper accounting methods.[3] On this record we could not make such a finding.

[fol. 84] Accordingly, we find that the accrued depreciation and depletion to be deducted in determining the rate base for 1952 is $18,182,793.

Working Capital.

Both the Company and staff computed the allowance for Working Capital in the same manner, the difference of $106,260 being due to the fact that the sum used for operating expenses by Colorado in computing cash Working Capital (as 1/8 of operating expenses less purchased gas and certain other deductions) exceeded that used by the staff

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[3] Interstate Power Company, 2 F. P. C. 71, 82. Hope Natural Gas Company, 3 F. P. C. 150, 168.

by the amount of $850,080. Based upon our determination as hereinafter set forth of the appropriate sum to be allowed for operating expenses we find that the amount of Working Capital before applying any adjustment for advance collection from customers by Colorado of sums to cover Federal income tax obligations to be $2,078,235. The staff did not make any adjustment for such advance tax collections. Under the staff's recommended reduction in rates no Federal income tax liability would be incurred by Colorado. Since, however, the determinations which we have made herein will result in Colorado's having a Federal income tax liability, it is appropriate that the principles which we have enunciated in the recent cases[1] be applied in the instant proceeding. We find that Working Capital as computed above of $2,078,235 should be reduced by $139,199 which is 75% of the Federal income tax of $185,599 which tax we find would be appropriate for the year 1952. Thus the appropriate Working Capital allowance becomes $1,939,036 instead of $2,054,694 shown on page 4.

We, therefore, find that the rate base of Colorado for the year 1952 upon which it is entitled to earn a fair return is $57,048,988 instead of $57,164,646 as shown on the same table.

[fol. 85] Operating Expenses

Colorado's claim for operating expenses during the test year exceeds the recommended allowance by the staff for such item in the amount of $864,973. Of this amount, $810,517 represents alleged increases in operating costs which were not presented by Colorado as part of its case in chief but which were submitted after the staff concluded its rebuttal evidence. Various elements comprising the difference of $864,973 are discussed below.

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[1] In the Matter of Alabama-Tennessee Natural Gas Company, Opinion No. 226, April 30, 1952.

In the Matter of Transcontinental Pipe Line Company, Opinion No. 227, May 29, 1952.

Wages and Salaries—$342,529.

To the original claim for salaries and wages of $2,717,705 for 1952, which claim was accepted by the staff, Colorado has added estimated increased wages and salaries of $342,529. Such amount is of two categories, each computed in a different manner Colorado first took the January, 1952, payroll for general officers and general office employees added 4% thereto and multiplied the result by 12 to arrive at an annual cost of $670,092. This amount is $165,481 in excess of the annual amount originally claimed by the company and accepted by the staff. The above-mentioned 4% was added to take care of projected future increases in wages and salaries during the year 1952. Admittedly, the added 4% is not a cost being currently incurred or that can reasonably be projected for the future. Indeed it is purely speculative and conjectural.

The record also shows that the payroll for the month of January includes some overtime pay arising from the merger with Canadian River Gas Company which became effective January 1, 1952. The record does not support the assumption that this one month's experience by itself is a sufficient guide to measure the cost of general officers and general office employees salaries for the year 1952.

But the record shows that effective January 1, 1952 a cost of living increase of 4.16% was given to employees in these classifications. This increase in salaries should be recognized and we, therefore, increase the original claim by the amount of $20,992 based upon the 4.16% of the amount originally estimated.

[fol. 86] Colorado increased the salaries and wages paid to other classifications of employees over the original estimate by an amount of $177,048. This amount is 8% of the salaries and wages originally claimed for 1952. The record shows that effective January 1, 1952, Colorado did grant its employees in these classifications a 4% average increase in wages and salaries. This amount is computed at $88,524, which sum we add to the original claim.

The projected second 4% increase is, like the similar item mentioned above, a speculative and conjectural increase. We are here allowing all increases in wages and

salaries which are supported in this record. We do not, however, deem it our responsibility or duty to speculate as to what future wage increases, if any, may be granted by Colorado. For the foregoing reasons we find that Colorado's claim for an allowance for wage increase of $342,529 must be rejected except for the sum of $109,516 which we allow.

Employees' Welfare Expenses and Pensions—$306,727.

Colorado has included in its cost of service estimated increases for Employee Benefits consisting of $14,816 for Group Hospitalization $13,887 for Group Life Insurance, and $278,024 for Pensions. While the employees of Colorado are not presently enjoying any of these proposed benefits nor is Colorado incurring any of the proposed costs we are asked to allow them on the assertion that unless we do these benefits could not be undertaken or if undertaken would reduce Colorado's return below the amount allowed. It has been our consistent policy to make full allowance in rate proceedings for all costs of Employees Benefits actually incurred and we do so here. We would unhesitatingly allow these particular items if there were any reasonable degree of certainty as to their effectiveness but no such assurance was given upon this record. Moreover, it was admitted unequivocally by the company's witness that these Employee Benefits proposals are purely in the planning stage.

In reference to the Employees' Welfare and Pension Plans, Colorado made the following statement in a regis- [fol. 87] tration statement and prospectus filed with the Securities and Exchange Commission on April 2, 1952 and which is in this record:

"During 1951 employees paid approximately $87,600 under these several plans, while the company's payment approximated $115,400. *Under the present plans it is not anticipated that there will be an appreciable increase in cost in 1952.* Consideration is being given to revisions in the Group Life Insurance Plan, Group Hospitalization and Surgical Benefits Plan and Retirement Plan, so as to provide increased benefits under these plans. The possible revisions being considered might increase the cost of such

plans to the company by as much as $307,000 during 1952, *but the Board of Directors has not yet come to any conclusion as to the adoption of any such revisions.*" (Emphasis supplied.)

In the face of such statement, it is not reasonable to burden the rate payers with a substantial item of cost when such costs are not in fact being incurred and when there is no evidence in the record to indicate when such costs would be incurred.

If, in the future, this question of employee benefits be resolved by management and its employees the way is open under the Natural Gas Act for the recovery through rates of such additional costs as may be actually experienced. Assuming no great lapse of time occurs before the question is resolved, all of the facts in the instant proceeding will be before the Commission and it can act promptly upon the request of Colorado when made.

We, therefore, reject Colorado's claim for estimated increases in Employees' Welfare Expenses and Pensions in the amount of $306,727.

Director and Executive Committee Payments—$75,000.

In its revised cost of service computation for 1952, Colorado [fol. 88] has included the amount of $75,000, representing $5,000 fees for each of its Directors who are not full time employes of the company; $30,000 for the Chairman of the Executive Committee and $15,000 for other members of the Executive Committee who are not full time employees of the company, such payments to become effective April 1, 1952.

The fees in question were authorized at a special meeting of the Directors of Colorado held on March 10, 1952 at 30 Rockefeller Plaza, New York City. Four of the seven[5] Directors were present: Messrs. Joseph H. King, Robert W. Hendee, F. T. Parks and W. A. Dougherty.[6]

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[5] Two directors were absent and there was one vacancy.

[6] Mr. King is a Director and President of the Union Securities Corporation, 65 Broadway, New York City; Mr. Hendee is President of Colorado Interstate, Colorado Springs, Colorado; Mr. Parks is a Director and Vice Presi-

At the aforesaid meeting the Board approved the filing, with the Securities and Exchange Commission, of a Registration Statement covering the sale of 971,480 shares[7] of Colorado's common stock par value $5.00 per share owned by the Union Securities Corporation group[8] and Sinclair Oil Corporation. Prior to such sale the Union Securities group owned 42½% of Colorado's common stock acquired in 1947 from Standard Oil Company (N. J.) Southwestern Development Company owned 42½% and Public Service Company of Colorado owned 15% of Colorado's common stock.

Sinclair Oil Corporation acquired 21.69% of Colorado's stock by reason of its ownership in Southwestern Develop- [fol. 89] ment Company[9] and the Mission Oil Company

dent of the Public Service Company of Colorado, Denver, Colorado, the largest resale customer of Colorado Interstate; Mr. W. A. Dougherty, 30 Rockefeller Plaza, New York City, is the Vice President and General Counsel of Colorado.

[7] The stock was initially registered on the basis of the sale of 966,000 shares; however, it appears that the Underwriters actually sold an aggregate of 988,905 shares at the public offering price of $26.75 per share—22,905 shares having been oversold on allotments. The several Underwriters covered their short position by purchasing 13,688 shares from Sinclair Oil Corporation and the remaining shares upon the open market.

[8] This group consists of Union Securities Corporation, A. C. Allyn & Co., Inc., Equitable Securities Corporation and Stifel Nicolaus & Co. Inc.

[9] By order of December 21, 1951 the Securities and Exchange Commission approved a plan of corporation simplification relating to Sinclair, Southwestern Development Company and The Mission Oil Company under Sec. 11 of the Public Utility Holding Company Act of 1935. Among other things the plan provided for the sale to the public of the common stock of Colorado Interstate to be acquired by Sinclair as the result of its holdings of 51% of the common stock of Southwestern and 3.98% of the common stock of The Mission Oil Company which in turn owned 47.28% of the stock of Southwestern.

acquired 20.11% of Colorado's stock also by reason of its ownership in Southwestern. As a result of the public sale on April 2, 1952 of Colorado's stock, Sinclair Oil Corporation no longer holds any of such shares and the Union Securities group apparently now owns only 126,449 shares out of the 726,757.05 shares originally held.[10]

Prior to the foregoing action of March 10, all Directors of Colorado received an attendance fee of $50.00 per meeting plus expenses. This fee was increased to $100.00 per meeting by the Board at the March 10 meeting and in addition the Board, with one of the four members present dissenting,[11] voted to give each Director, not a full time employee of the company, $5,000 per year for his services.

At the same meeting, the Directors elected three of their number to a newly created Executive Committee, two of whom were representatives of Union Securities Corporation and Sinclair Oil Corporation respectively. Whereas previously, members drew no separate compensation for their services on the old Committee, the Board over the opposition of the same member voted to fix the compensation of those members not full time employees of the company at $30,000 annually for the Chairman and $15,000 for other members. The representative of Union Securities Corporation was made Chairman.

At a further meeting of the Board of Directors of Colorado held on May 16, 1952, at the offices of the Company in [fol. 90] Colorado Springs, Colorado, at which six of the seven Directors were present,[12] it was noted on the minutes that the representative of Sinclair was no longer a member of the Board of Directors of Colorado due to a requirement of the Securities and Exchange Commission that such

[10] Union Securities Corporation sold 345,176.43 shares out of a total owned of 362,865.52.

[11] Mr. F. T. Parks, Director and Vice President of Public Service Company of Colorado.

[12] Mr. Parks was absent. Mr. William G. Mariner, President of Mississippi River Fuel Corporation of St. Louis, Missouri, was elected, to fill the vacancy existing at the time of the March 10 meeting prior to the May 16 meeting.

representative resign upon the sale by Sinclair of the Colorado common stock received from Southwestern Development Company.

At the meeting of May 16, Mr. W. A. Dougherty replaced the Sinclair Oil representative on the Executive Committee. The Board also increased the annual salary of Mr. Hendee at this meeting from $36,000 to $45,000.

In the calendar year 1951, Colorado expended for salaries of its general officers and executives the sum of $73,714 while Canadian River Gas Company expended $33,929.30, or a total for the two corporations combined of $107,643.30. The amount originally estimated by Colorado for the year 1952 as compensation for its general officers was $103,889, thus the increases voted by the Board of Directors represent better than an 80% increase in the cost of executive direction of this utility.

The action by a minority of the authorized Board in voting themselves and absent Directors additional compensation to be effective one day prior to the public sale by their principals of most of their holdings of Colorado's common stock detracts greatly from Colorado's claim that "it is reasonable to contract for the services of men competent to forward the welfare of the company."

The action of Union Securities Corporation in placing its President, Joseph H. King, in an advantageous position to direct the affairs of Colorado just before it disposed of sub- [fol. 91] stantially all of its holdings of Colorado's stock is reminiscent of the Holding Company era involving investment banker control of public utilities through interlocking director.

In the face of these circumstances justification for such a large increase in cost, claimed on rebuttal when the hearing was on the verge of completion, was plainly required of Colorado. It was not enough for Colorado to simply assert that such fees were legally authorized; that it is reasonable to presume that those who will receive the fees will earn them, and that the future will fully vindicate the compensation of the Directors and Executive Committee members.

On this record, we cannot find that the reasonableness of these fee payments (of $75,000) has been established. We, therefore, find that such payments may not be included as a

part of Colorado's cost of service to be recovered through rates subject to our jurisdiction.

Royalties—$86,261.

Colorado claimed payments of gas royalties for the test year of $1,422,730 which is $86,261 in excess of the amount originally estimated by Colorado and accepted by the staff. The revised estimate was premissed upon settlement of a royalty controversy involving approximately 8% of the gas produced by Colorado in the West Panhandle field. A royalty rate of 1/8 of 8¢ per Mcf at 14.65 psi. was then applied by the company witness to all gas produced,[13] on the assumption that the company would have to pay this higher rate in the future to all royalty owners.

It is indisputable that the additional amount claimed for gas royalty payments at the time of hearings did not represent actual experience or contractural obligations. Certain events have transpired, however, since that time which lead us to the conclusion that such additional royalty payments have been removed from the realm of specula-
[fol. 92] tion. It appears that two additional law suits involving gas royalties have now been settled and that the Board of Directors, on May 16, 1952 authorized the management to negotiate with the other royalty owners on the same basis. For this reason, we allow the additional claim of $86,261 for gas royalties.

V. Regulatory Commission Expense—$54,456.

The amount of regulatory Commission expense claimed by Colorado is $93,593 detailed as follows:

Regulatory expense per books, year ended September 30, 1951		$23,593
Estimated expense Docket No. G-1115 before FPC	$42,780	
Estimated Cost of Court review	95,000	
Total estimated cost of rate base	$222,780	
Amortization over approximate 4-year Period		70,000
Total Company claim		93,593

[13] The record shows that approximately 50% of the royalties were being paid on the basis of 1¢ per Mcf which were included in the original estimate of Colorado Interstate and accepted by the staff.

The staff recommended three adjustments to the company's claim as follows:

(1) Included in the Regulatory Commission Expenses, which were recorded in Colorado's books for the year ended September 3, 1951 is a $10,000 fee paid to Price Waterhouse & Company for the services of D. F. Houlihan who testified in behalf of Colorado in the merger proceeding, Docket No. G-1326. The staff eliminated such item as nonrecurring. Colorado takes exception to the adjustment on the basis that while this particular item might not be experienced again, other items of cost would occur in its place. Colorado's theory would involve an allowance based on speculation, a basis which has been repeatedly rejected by this Commission (Cities Service Gas Co. 3 F. P. C. 459, 485). Moreover, no evidence was presented to show that the remaining amount of Regulatory expense, i.e., $13,503 was inadequate on the basis of past experience or for future [fol. 93] requirements. Accordingly the Houlihan fee is eliminated.

(2) The claim of $95,000 by Colorado as the estimated cost of seeking Court review of our Order in this proceeding is entirely speculative and conjectural and we think not properly includible as part of the cost of service. (Driscoll v. Edison Light & Power Co., 307 U. S. 104, 121). It is, therefore, rejected.

(3) Colorado amortized its Regulatory Commission expense applicable to this case over an approximate 3-year period, whereas the staff used a 5-year period. As we stated in the previous Colorado rate case, "It is customary to amortize such expenses over a period of 5-years or more." 3 F. P. C. 32, 55. No new significant facts appear here which would warrant a departure from the customary rule. Alabama-Tennessee Natural Gas Company, Docket No. G-585, Opinion No. 226, Page 13, April 30, 1952. We, therefore, use a 5-year period of amortization.

Depreciation and Depletion—$140,934.

We have heretofore discussed the above item under Rate Base, page 5. Suffice it to say here we find the annual provision for depreciation and depletion for the test year to be $2,595,427.

Taxes Other Then Federal Income Taxes—$63,765.

The above amount relates to the State income taxes. The computation of such tax is geared to the amount of Federal income taxes allowed. Therefore, upon the basis of the computed Federal income tax liability as described in the Section next following, we find the appropriate amount to be allowed for State income taxes to be $5,568.

Federal Income Taxes—$2,306,808.

Federal income taxes are computed on the basis of return allowed and the various tax deductions to which Colorado is entitled. For this reason the amount allowable for Fed- [fol. 94] eral income taxes is the end result of other determinations of costs includible in the cost of service and of the appropriate tax deductions.

Colorado claims deductions for Federal income tax purposes of $1,578,089 whereas the deductions computed by the staff total $2,700,602. The differences are:

Depreciation per books	$ 140,934
Depletion—Tax return basis	981,579
Total	$1,122,513

We have dealt previously with the difference of $140,934 in the annual provision for depreciation and no further attention thereto at this point is required.

As for the $981,579, in computing the depletion allowance for Federal income tax purposes, Colorado used 3.17¢ per Mcf as the wellhead value of the gas produced by it in the West Panhandle field. The staff used a wellhead value of 5¢ per Mcf, the depletion allowance thereunder for tax purposes being $1,379,972 as compared with the allowance claimed by Colorado at the 3.17¢ value of $398,393. Under the tax code a producer of natural gas is permitted an annual deduction for depletion amounting to 27½% of the wellhead value but not to exceed 50% of the net income. Without going into the mechanics of the so-called percentage depletion allowance it is sufficient for our purposes here to state that generally speaking the higher the well-

head value the greater the depletion allowance; the greater the depletion allowance the lesser the Federal income taxes; and the lesser the Federal income taxes the lower the cost of service.

The 5¢ per Mcf wellhead value was used by the staff in the instant proceeding because that was the value claimed by Colorado to support its application for a certificate of public convenience and necessity authorizing the merger into it of Canadian River at Docket No. G-1326. In that proceeding Colorado presented evidence to show that if a merger were authorized Colorado would be able to receive an increase in the wellhead value above the 3.17¢ which [fol. 95] was the basis of the last settlement by the Bureau of Internal Revenue for the 1945 tax year. It was stated that such higher wellhead value would be at least 5¢.

To show that the merger would be in the public interest, Colorado relied upon the substantial savings in Federal income taxes which would be brought about by an increased depletion allowance to offset the loss in revenues derived from the sale of liquid hydrocarbons which, under the merger, would be diverted in large part to Southwestern Development Company or its nominee. In the merger proceeding the company placed in evidence Exhibits which showed that, based upon a 5¢ wellhead value for depletion purposes and a 45% Federal income tax rate, the total tax benefit to Colorado Interstate for the period 1950-1972 would be $14,324,415. This same evidence is before us in this proceeding. Colorado has alleged no new facts nor are there any facts showing any change from the facts and testimony introduced by it in the merger proceeding. We conclude that the same evidence which supported and warranted our finding that 5¢ was a reasonable figure for tax depletion purposes supports and warrants a similar finding here. As a matter of fact, on April 24, 1951 Colorado filed an application for a certificate of public convenience and necessity at Docket No. G-1677 authorizing the construction and operation of additional facilities and in that application it included an income statement in which the depletion allowance for tax purposes was taken at the 5¢ wellhead value.

In our Opinion No. 209 (Decided March 20, 1951) authorizing the merger we had the following to say concerning the evidence which was there presented:

"As against this cost [the loss of the hydrocarbons] Colorado stands to gain an estimated $14,324,415 in tax benefits becoming available to the merged company by reason of the transfer to it of the percentage depletion allowance based on the production of both natural gasoline and natural gas from Canadian's acreage. We think that the [fol. 96] weight of the evidence supports this forecast in tax savings. Such savings clearly will inure to the benefit of Colorado's customers and the consumers of the Rocky Mountain area.

* * * We cannot and do not here attempt to influence the depletion allowance ruling which will be made by the Bureau of Internal Revenue, but, from this record, we think that the basis upon which the tax savings of Colorado of $14,324,415 was estimated is a reasonable one." (Brackets supplied.)

While Colorado has insisted throughout the present proceeding that it is going to prosecute vigorously before the Bureau of Internal Revenue its claim for a depletion allowance of at least 5c per Mcf, it takes the position that until such decision is finally realized the value of 3.17c should be used in this proceeding.

We think Colorado's proposal is without merit after its representations made to us in the merger proceeding. Further, Colorado in equity and good conscience is estopped to deny the 5c value here. The tax credits which would redound to Colorado and its customers as a result of a merger were a necessary ingredient to our authorization thereof. Not only is Colorado retaining the benefits of the certificate which we issued at Docket No. G-1326 but Southwestern's nominee is receiving the liquid hydrocarbons given up by Colorado pursuant to the merger agreement estimated to amount to $1,428,780 for the year 1952. Such revenues would have effected a reduction in the cost of service of such amount had the merger not taken place.

That Colorado, in the merger proceeding, fully understood and intended that the tax credits should offset the loss

in gasoline revenues and that the merger would not result in any additional costs to be borne by the rate payers cannot be disputed. Its effort in this proceeding to negate its prior representations and positions, thereby substantially increasing the cost of service cannot be justified. We would [fol. 97] be derelict in our duty were we to follow Colorado's pleadings and allow the cost of service to be thus increased. Accordingly, we shall compute the depletion allowance for Federal income tax purposes at 5c per Mcf in lieu of 3.17c proposed by Colorado. On such basis we find the proper allowance for Federal Income taxes to be $185,599, as shown by the following table:

Colorado Interstate Gas Company

G-1115

Computation of Federal and State Income Taxes Year 1952

Gas Service Revenues, as Estimated	$17,962,532	
Less: Excess Revenues	3,009,965	$14,952,567
Revenue from Gasoline Operations		1,104,020
Other Gas Revenues—Rent		37,500
Total Income		16,094,087
Deductions:		
Operating Expenses	$ 613,484	
Statutory Depreciation	2,327,417	
Statutory Depletion (Adjusted for Increased Royalties)	1,356,251	
State Income Taxes	5,568	
Taxes—Other	1,835,229	
Intangible Drilling Costs	585,920	
Cost of Removal	26,395	
Interest on Long-term Debt	963,309	
Amortization and Sundry	12,025	15,726,589
Normal Tax Net Income		367,498
Less: Surtax Exemption		25,000
Surtax Net Income		$ 342,498

[fol. 98]

Federal Income Tax:	
Normal Tax at 30%	$ 110,249
Surtax at 22%	75,350
Total	$ 185,599
State Income Taxes:	
Computed as 3% of Federal Income Tax	$ 5,568

Rate of Return

The rate of return claimed by Colorado is 6½%. The staff contends that a return of 5¾% is fair, reasonable and proper based upon the record in this proceeding. Since the difference between the staff and company as to rate base is only $35,794, the difference in return of $431,061, shown by the tabulation on page 4, is due almost entirely to the difference in the rate of return. We have in this record an abundance of evidence on the subject of rate of return including average yields for bonds of public utilities, railroads and industrials as well as U. S. Treasury bonds; data on public offerings of natural gas bonds, preferred and common stocks; earnings-price ratios of various natural gas companies' common stocks; natural gas companies' capitalization ratios and data as to Colorado's outstanding securities, its earnings and financial requirements.

The capitalization of Colorado as of December 31, 1951, which is similar to the industry as a whole and which we find to be reasonable, is as follows:

		Amount	Percent
Long-term Debt		$29,600,000	53.9%
Preferred Stock		2,000,000	3.6%
Common Equity			
Common Stock (1,711,016.6 shares) [fol. 99]	$ 8,555,000		
Surplus	$14,759,000		
		$23,314,000	42.5%
		$54,914,000	100.0%

The outstanding long-term debt of Colorado consists of four issues of long-term serial notes as follows:

2% Notes, due $400,000 semi-annually May 1, 1952 through May 1, 1954	$ 1,200,000[1]
2¾% Notes, due $400,000 semi-annually November 1, 1954 through November 1, 1964	$ 8,400,000
3⅛% Notes, due $250,000 semi-annually October 1, 1952 through April 1, 1960	$ 8,000,000
3¾% Notes, due $400,000 semi-annually February 1, 1955 through August 1, 1969	$12,000,000

[1] Excludes $800,000 of such notes due within one year included in current liabilities.

The weighted average cost of such debt is 3.21%. The outstanding preferred stock of the company bears a dividend rate of 6%.[15] Colorado agrees that the actual cost of its long-term debt and preferred stock capital is as shown above but maintains that such costs do not take into consideration future needs in attracting new capital.

It is, of course, true that the most recent issue of notes sold by Colorado bears an interest rate of 3¾% which rate exceeds the average rate of 3.21% for all of its outstanding long-term debt. It may well be that Colorado, in the indefinite future, may find it necessary to incur a higher interest cost than the average rate it is now paying in order to raise additional debt capital. But Colorado's contention presupposes that rate making is not a continuing process and that appropriate adjustments of rates cannot be made when experience demonstrates that adjustment is required. We find that the actual cost of the company's outstanding long-term debt and preferred stock is a proper [fol. 100] measure of the cost of borrowed money and of preferred stock funds in determining a fair rate of return for Colorado in this case.

Colorado strongly urges that it is entitled to a return on its equity capital of 11%, and bases such claim upon the testimony of its witness Merrill that such rate of return is necessary if the company is to be able to maintain its credit and attract capital. Mr. Merrill's 11% return for common equity was derived from selected earnings-price (net price to company) ratios of eight natural gas utility common stocks which were issued and sold between February 1948 and October 1951.[16] The record shows that these

[15] The company has stated to the Securities and Exchange Commission that it will retire such presently outstanding stock on or before December 31, 1952.

[16] Three publicly offered issues of Tennessee Gas Transmission Company and one of American Natural Gas Co. with low earnings-price ratios were eliminated because according to the witness these companies had not developed their full earning power. He also eliminated one 1948 issue of Pacific Lighting Corporation which he considered on the high side.

earnings-price ratios used by the witness were, with one exception, based on offerings to stockholders rather than to the public and thus were made at a considerable discount under prevailing market prices. It is generally recognized that such type of offerings do not represent the best prices that these companies could have received and, therefore, the results obtained therefrom cannot be wholly relied upon in determining the investor's appraisal of the cost of equity capital.

An objective study of the investors' appraisal of the common stock of nine natural gas companies [17] held by the public indicates that during the five years ending August 1951 investors have been requiring a return on the average on the issues sold publicly of around 8.3%. The average earnings-price ratios of the outstanding common stocks of seven natural gas companies traded on recognized exchanges for the same period was 8.2% with the average for the last 12 months of such period being 7.5% and decreasing to 6.4% at October 1951. At the latest date shown by the record, July 1951, the yields varied from 3.5% to 6.4%. [fol. 101] Persuasive evidence as to the cost of equity capital is provided by the experience of Colorado itself. On April 2, 1952, just two days prior to the conclusion of the hearings in this Docket, two of the principal stockholders' groups of Colorado offered for sale to the public 966,000 shares of Colorado's common stock held by them. This was the first public offer ever made of Colorado's stock and the amount offered represented 56% of the total common stock outstanding. As previously noted in this Opinion, the record shows that the public offering was oversold. The stock was offered at $26.75 per share to net the selling stockholders at $25.25 per share. The book value of the stock as of the most recent date available preceding the sale (December 31, 1951) was $13.63 per share. Based on earnings for 1951 of $1.88 per share the earnings-offering price ratio is 7.03% and the earnings-net price to the selling stockholders ratio is 7.44%.

[17] Natural gas companies reporting to the Federal Power Commission.

Colorado attempts to discount the earning-price ratio resulting from the public sale of its stock, maintaining that the investors might have been willing to take a smaller return because of potential development of future earning power as a result of the merger. While the price which the investors were willing to pay for the common stock of Colorado may have been based in some degree upon the investors' appraisal of the growth possibilities of the merged corporation, it can be argued that the investors also took into consideration the instant rate proceedings and the substantial reduction in income available for common stock which might result therefrom, mention thereof having been made in the company's Prospectus. It can only be concluded from the results of the sale that the selling stockholders were competing for the investors' dollar and likewise the investors were competing for Colorado's stock at the price at which it was offered. Under such circumstances the verdict of the market place is compelling evidence.

[fol. 102] A rate of return of 5¾% on the rate base which we have here used would provide a return for the common stock equity of Colorado of 8.45% [18] after the servicing of its debt and preferred stock requirements and after allowance for all income taxes. Such return for equity capital is, we believe, wholly adequate in the light of the record in this case.

We therefore conclude and find that based on the record in this proceeding a rate of return of 5¾% is fair, reasonable and adequate to assure confidence in the financial soundness of the utility; to maintain its credit and to enable it to attract capital necessary for the proper discharge of its public duties. [19]

[18] After allowance for cost of financing of ½%.

[19] F. P. C. v. Hope Natural Gas Company, 320 U. S. 591, 601, 603; Bluefield Waterworks & Improvement Company v. Public Service Commission, 262 U. S. 679, 692-693; United Railways v. West, 280 U. S. 234, 261-262.

Loss on Gasoline Operations

In issuing a certificate of public convenience and necessity at Docket No. G-1326 authorizing Colorado to acquire the properties of Canadian River, we attached the following condition:

"The authorization herein granted for effectuating the acquisition and operation of Canadian's properties and facilities is upon the express understanding and condition that if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenue to be received by Colorado from the hydrocarbons resulting from the operation of Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pursuant to such transaction, then and in that case in any proceed-[fol. 103] ing in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers."

There is no dispute that this condition was a reasonable one in the light of the record at Docket No. G-1326 and required by the public convenience and necessity. Colorado pursuant to the order issuing the certificate at Docket No. G-1326 has duly accepted the certificate and the conditions thereto attached. Nor is there any dispute as to the meaning and intent of the above-quoted condition. The question arising here is the determination of "the costs properly allocable to such hydrocarbons."

Under the merger agreement, as referred to in the above mentioned condition, Colorado has agreed to produce, gather and process liquid hydrocarbons, contained in the wet gas stream, and turn over the finished natural gasoline to Southwestern Development Company or its nominee at the loading rack of the Bivins and Fourway gasoline plants operated by Colorado in the West Panhandle field. Upon

the consummation of the merger, Southwestern denominated Westpan Hydrocarbon Company (Westpan) as the owner of the hydrocarbons and to whom delivery is to be made. Westpan in turn, sells the finished gasoline, and after deducting ¼th cent per gallon as cost of marketing, remits 50% of the gross revenues to Colorado. Additionally some of Westpan's liquid hydrocarbons are processed at the Fritch Gasoline Plant, owned and operated by Natural Gas Pipeline Company of America (successor to Texoma Natural Gas Company). The wet gas is produced and gathered by Colorado, brought by it to the Fritch Plant; processed there, the dry gas being sold by Colorado to Natural Gas Pipeline Company, that company sells the finished gasoline, deducts its actual costs of operation and marketing, and remits the balance to Colorado pursuant to agreement with Colorado. Under the merger agreement, Colorado agreed to remit to Southwestern or its nominee 85% of such net proceeds from the Fritch plant operations. [fol. 104] It remains, therefore, to determine whether the 50% of the gross revenues received by Colorado from the gasoline operations at the Twins and Fourway plants, and the 15% received by it from Natural Gas Pipeline Company cover the costs properly allocable to the producing, gathering, and processing of the liquid hydrocarbons. Indeed, our opinion at Docket No. G-1326 recognizes that the "costs of producing, gathering and extracting the natural gasoline" are to be considered. (Opinion No. 209, page 8.)

Colorado claims that the gasoline revenues which it receives under the merger agreement exceed the costs properly allocable to its gasoline operations in the Panhandle field by $624,985. The staff, however, contends that such revenues fall short of meeting the cost of producing and processing the gasoline by an amount of $585,528. We have not heretofore been concerned with a similar problem since it has not been necessary under our policy in rate cases to separate the costs associated with the production and processing of gasoline from total production cost as we have always included in the cost of service all costs and revenues applicable to the gasoline operations of a natural gas company. Thus, for the purpose of the instant pro-

ceeding we find it necessary to test opposing theories and to resolve wide differences of opinion and results.

It is recognized by both Colorado and the staff that inasmuch as the liquid hydrocarbons are contained in the wet gas stream the cost of producing and gathering such wet stream to the inlet of the gasoline plants is a joint cost. The method of allocating such joint cost is one of the most important questions to be resolved. The staff allocated the joint wellmouth and gathering costs on the basis of the relative market value theory of joint production, a method generally employed in the petroleum industry. Under this method the joint costs are apportioned to the finished product on the basis of the relative market values of such products. The direct costs incurred to make each product fully marketable are deducted from the respective market [fol. 105] values of the finished products so as to determine relative market values at the point of processing where joint operations cease.

For the respective market values the staff recommended and used 5 cents per Mcf as the value of the dry gas, and as the value of the gasoline the total gasoline revenues for 1952 as estimated by Colorado, less the direct cost to make the gasoline marketable and other direct gasoline costs. The five cent value for the dry gas was based on the then latest reports of the Texas Railroad Commission as to the weighted average market price at the wellhead paid for gas being used and sold in the Panhandle field. The report of September 12, 1951, based on evidence submitted at a hearing before that commission states that the Texas Railroad Commission finds that the weighted average wellhead price being paid in the Panhandle field is 4.8526 cents per Mcf measured on a 16.4 pressure base. Further, Colorado or its predecessor, Canadian River, paid the Texas production tax based on the market value of its gas at 4.33 cents per Mcf. The staff assigned all the costs of the gasoline plants to the gasoline operation, except such costs as applied to the steam and cooling facilities to dehydrate the gas entering Colorado's transmission line.

Colorado, on the other hand, allocated the wellmouth and *and* gathering costs on what it termed a volumetric method based on the shrinkage of the wet gas volume while being

processed. The result of such method is that one per cent of the total wellmouth and gathering costs of the wet gas processed at the Bivins and Fourway plants is assigned to gasoline and 99 per cent to the dry gas. Because the contract with Natural Gas Pipeline Company for the processing of the wet gas at the Fritch plant provides for a 2 per cent shrinkage allowance, Colorado allocated 2 per cent of the total wellmouth and gathering costs of the Fritch gas to gasoline and 98 per cent to dry gas. The weighted average percentage of all the wellmouth and gathering costs for all the wet gas processed at the three plants results in 1.27 per cent assigned to gasoline and 98.73 per cent to dry gas. Thus, of $4,323,547 claimed by Colo- [fol. 106] rado as total wellmouth and gathering costs for all the wet gas processed at these three plants, Colorado assigns $55,008 as the cost attributable to the gasoline operations, and the balance to the dry gas.

Colorado, additionally, treats the processing [20] of the wet gas within the gasoline plants up to and including the distillation unit as a joint operation. The balance of the processing is treated as a direct gasoline operation, except for an amount allocated to the dry gas for dehydration. In spreading the gasoline plant costs which it considers joint, Colorado used the same 1 per cent and 2 per cent basis which it used for the wellmouth and gathering costs. The result is that out of total claimed costs of $1,012,603 for operation of the three gasoline plants, Colorado claims $570,617 as joint costs, $366,374 as direct gasoline costs, and $75,612 as direct dry gas costs. Then Colorado assigns

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[20] In brief, the processing involves bringing the wet gas in contact with mineral oil in vessels termed "absorbers." The heavier hydrocarbons in the wet gas are picked up by the mineral oil—such oil being circulated in a continuous process through the absorbers and in a distillation unit, the liquid hydrocarbons being separated from the oil in the latter. The liquid hydrocarbons are further processed through a stabilizer and gasoline treater to bring them to a commercial marketable grade of natural gasoline. The dry or residue gas stream flows from the absorbers to a dehydration unit and thence into the pipe-line system.

$7,453, or 1.27 per cent, of the $570,617 joint costs to the gasoline and the balance of $563,164, or 98.73 per cent, to the dry gas. Thus a total of $638,776 ($563,164 of joint costs plus $75,612 of direct costs) is assigned to the dry gas and $373,827 to the gasoline operations out of total gasoline plant costs of $1,012,603.

Colorado contends that the relative value method is subject to such serious deficiencies upon application to the facts in this case that it breaks down. On the other hand the staff urges that the volumetric basis fails to recognize the economics of the natural gasoline business and produces an unreasonable result. We believe the Supreme Court of the United States cogently stated the criteria to be applied in allocation matters when it said, "considera- [fol. 107] tions of fairness not mere mathematics govern the allocations of costs." Colorado Interstate v. F. P. C., 324 U. S. 581. Moreover, the reasonableness of the result is essential to the validity of any method of allocating joint costs. Accounting for Joint Costs, Harold G. Avery, Accounting Review, April 1951.

We think neither the relative value method, nor the volumetric method are entirely satisfactory, but from our study of the evidence we are of the opinion and find that the relative value method as applied by the staff produces a more reasonable and fairer result in our judgment than does Colorado's method. The record shows that during the year 1952 it is estimated that 45,143,140 gallons of natural gasoline will be processed at the three plants, the total market value of such gasoline being estimated at $2,482,600. This amount must be compared with the total costs assigned to natural gasoline operations by Colorado of $428,835. Thus, it is evident that the annual revenues from the sale of natural gasoline exceed by more than five times the costs allocated by Colorado to such operations after allowance for a return of 6½% and the income taxes associated therewith. On a rate of return basis, the method followed by the staff would result in the gasoline operations earning a 15.8% rate of return on the rate base assigned to such operations as compared to a rate return resulting from Colorado's method of 163%.

We next turn to the allocation methods and cost assignments within the gasoline plants themselves. As previously noted, the staff assigned all of the costs associated with the gasoline plant operation directly to natural gasoline other than those applicable to the dehydration of the pipe-line gas. Colorado, on the other hand, divided the gasoline plant facilities between (1) joint dry gas and gasoline; (2) direct dry gas and (3) direct gasoline, and assigned or allocated to these three classification operating expenses, depreciation, taxes and return.

It is the position of Colorado that it is necessary for the efficient operation of its transmission line system to extract the liquid hydrocarbons from the gas since unless [fol. 108] such liquids are extracted transmission line operations would be hampered and the lines would freeze up during low temperature conditions. The staff does not dispute that the removal of some liquids is necessary for operating purposes but maintains that the extraction of liquid hydrocarbons through Colorado's plants is carried on to a much greater degree than necessary for transmission line operations.

There is no doubt that under the merger agreement Colorado is obligated by contract to install the facilities necessary to extract gasoline as would be installed by a prudent operator. Furthermore, it may be required to extract the liquid hydrocarbons to a point where the remaining heat content of the dry gas would not be less than 963 Btu's per Mcf. Under such agreement, Colorado is not a free agent to discontinue or curtail its gasoline operations [21] to meet its transmission requirements and in fact may be called upon, under the merger agreement, to expand them substantially. It is admitted by Colorado's witness that if the gasoline operations were stepped up at the request of West Pan to produce more gasoline, the additional facilities would be chargeable wholly to the gasoline operations.

It also appears from the evidence that the dehydration unit serves to remove some liquids which are introduced

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[21] Colorado has authority under the agreement to by-pass the gasoline plants in cases of emergency.

into the gas stream during the course of its processing in the plants but all costs relating to dehydration were assigned entirely to dry gas. As we view the evidence some of the facilities which were assigned by Colorado to the joint gas and gasoline operations appear to be more properly assignable to the gasoline operations.[22]

From our examination of the record it is our conclusion that part of the operations of the gasoline plants should be [fol. 109] treated as a joint operation. We, therefore, adopt for the purposes of this case, Colorado's point of split-off within the gasoline plant and the percentages used by it to determine the joint gas and gasoline costs, the direct dry gas costs and the direct gasoline costs within the plants. We shall use, however, the gasoline plant costs heretofore found and determined by us to be the costs to be allocated. We also recognize that our adoption of Colorado's method may result in the assignment of more costs to the dry gas than may be proper but the record here does not include data for further refinement or adjustment.

Inasmuch as we find that the gasoline plant costs are in part joint costs, it becomes necessary to compute the market value of the raw gasoline at the point of split-off in the plants (at the conclusion of distillation process). Table I below shows the derivation of the representative market values of dry gas and natural gasoline and the resulting percentages to be used in allocating the joint costs to dry gas and natural gasoline.

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[22] For example, the "distillation unit" condenser and tank at the Bivins and Fourway Plants appear to be only necessary for the recovery of gasoline.

[fol. 110]

TABLE I

Colorado Interstate Gas Company

Computation of Percentages Used to Allocate Joint Gas and Gasoline Costs to Dry Gas and Natural Gasoline
Year 1952

	Total	Gasoline Plants		
		Bivins	Fourway	Eutch
Value of Dry Gas				
Gas Output of Plants—				
Mcf at 16.4 p.s.i.a.	113,682,214	49,893,969	20,864,638	42,923,607
Value of Dry Gas at 5¢ per Mcf	$5,684,110	$2,494,698	$1,043,232	$2,146,180
Value of Gasoline				
Gross Revenue	$2,482,600	$ 893,000	$ 457,000	$1,132,600
Less: Cost to Make Marketable (Direct Gasoline Plant Costs)	208,863	65,639	88,663	54,561
Value of Gasoline	$2,273,737	$ 827,361	$ 368,337	$1,078,039
Total Value	$7,957,847	$3,322,059	$1,411,569	$3,224,219
Dry Gas Percent		75.095%	73.906%	66.564%
Gasoline Percent		24.905%	26.094%	33.436%

[fols. 111-112] The allocation percentages as determined above are then applied to the joint wellmouth and gathering costs and to the joint gasoline plant costs as summarized in the Table below for each of the three plants:

(Here follows Table, folios 113-114)

Fols. 113-114]

TABLE
Colorado Interstate Gas Company
Allocation of Costs to Gasoline Operations and
Computation of Net Loss Thereon
Year 1952

	All Plants			Bivins		Fourway		Fritch	
	Total	Gas	Gasoline	Gas	Gasoline	Gas	Gasoline	Gas	Gasoline
Allocation Percentages				75.095%	24.905%	73.096%	26.094%	66.564%	33.436%
Joint Well Mouth and Gathering Costs	$3,921,979	$2,805,920	$1,116,059	$1,262,952	$ 418,854	$ 521,623	$ 184,170	$1,021,345	$ 513,035
Joint Gasoline Plant Costs (Note 1)	537,199	386,764	150,435	162,084	53,754	108,407	38,275	116,273	58,406
Total	$4,459,178	$3,192,684	1,266,494	$1,425,036	472,608	$630,030	222,445	$1,137,618	571,441
Direct Gasoline Costs (Note 1)			208,863		65,639		88,663		54,561
Total Costs Assigned to Gasoline			1,475,357		538,247		311,108		626,002
Applicable Gasoline Revenues			1,053,820		446,500		228,500		378,820
Net Loss on Gasoline Operations			$421,537		$ 91,747		$ 82,608		$ 247,182

Note 1
Segregation of Costs Within the Gasoline Plants Computed as follows:

	Total	Bivins	Fourway	Fritch
Total Costs Applicable to Gasoline Plants	$814,251	$301,431	$267,020	$245,800
Allocated as follows:				
To Joint Gas and Gasoline	$537,199	$215,838	$146,682	$174,679
Percent used for Operation and Maintenance Expenses		65.94%	48.80%	65.94%
Percent used for all other costs		78.51%	58.3 %	78.51%
To Direct Gasoline Costs	$208,863	$ 65,639	$ 88,663	$ 54,561
Percent used for Operation and Maintenance Expenses		26.21%	35.58%	26.21%
Percent used for all other costs		16.37%	31.9 %	16.37%
To Direct Dry Gas	$ 68,189	$ 19,954	$ 31,675	$ 16,560
Percent used for Operation and Maintenance Expenses		7.85%	15.62%	7.85%
Percent used for all other costs		5.12%	9.8 %	5.12%

[fol. 115] Thus, of the total wellmouth and gathering cost, $2,805,920 is allocated to dry gas and $1,116,059 to natural gasoline. The joint gasoline plant costs are allocated $386,764 to dry gas and $150,435 to natural gasoline. The gasoline plant costs directly assigned to natural gasoline amount to $208,863. The total cost therefore applicable to the production, gathering and processing of the liquid hydrocarbons owned by Westpan into finished gasoline is $1,475,357. The total revenue accruing to Colorado under the merger agreement for gasoline operations is estimated by it for 1952 to be $1,053,820. Therefore, from such operations there is a net loss or excess of cost over revenues of $421,537. Under the terms of the certificate which we issued to Colorado in Docket No. G-1328, supra, page 48, which terms and conditions were accepted by Colorado, this loss is not to be considered as a cost of service to Colorado Interstate's natural gas customers and consumers. Accordingly, we find and conclude that the loss of $421,537 shall not be considered as a part of the cost of service which we have heretofore determined.

In connection with our determination of the loss on gasoline operations it should be recognized that we are here adjusting the cost of service so as to remove the burden of such loss from the consumers as Colorado agreed should be done. We are not suggesting that Colorado set up cost accounting procedures for the purpose of currently segregating its cost on the basis of our decision as such appears to be entirely unnecessary.

Summary of Cost of Service.

Based upon the foregoing and the record before us we find that total overall cost of service is $14,952,567 as follows:

[fol. 116] Operating Expenses	$ 7,471,964
Depreciation and Depletion	2,595,427
Taxes Other than Fed. Income	1,840,797 [23]
Federal Income Taxes	185,599
Return at 5¾%	3,280,317
Loss on Gasoline Operations	(421,537)
Total Cost of Service	$14,952,567

Classification and Allocation of Cost of Service

One of the more important issues of this proceeding is the apportionment of the total cost of service between jurisdictional and non-jurisdictional sales. Both the staff and the company used the method of first classifying costs into demand and commodity classifications [24] and then al-

[23] We note from the press that a District Court of the State of Texas has held *unconstitutional,* the Texas Gathering Tax but that an appeal may be taken. The above amount of $1,840,797 includes the estimated Texas gathering tax for the Year 1952 in the amount of $573,332. Colorado is currently paying such tax under protest. It does not appear to us that we can make an adjustment therefor at this time, on the basis of these reports, but if Colorado is relieved from paying such tax we shall require a further rate reduction.

[24] The staff classified distribution costs between commodity and customer costs, rather than between demand and commodity. Colorado Interstate classified distribution costs between demand and commodity.

locating such classified costs among the various classes of customers. Both the staff and Colorado functionalized the cost of service into production,[25] transmission and distribution, functions. The only significant difference in method between Colorado and the staff in this respect relates to the assignment of Federal income taxes to functions. The staff assigned the total Federal income tax between functions on the ratio that the return calculated for each function bears to the total return. Colorado's method resulted in the assignment to the Panhandle field segment of the production function of a negative income tax which was utilized by Colorado as reducing the actual cost of the production functions. This is an unrealistic result. For the purpose of this case, therefore, we use the method recommended by the staff.

[fol. 117] The staff classified all production costs as a commodity cost. Colorado has assigned certain production costs or parts thereof, to demand on the theory that such costs do not vary with the volumes of gas produced. We find no justification in the record for treating these particular costs differently from the other production costs which Colorado admits should be classified to commodity. In re Northern Natural Gas Company, Opinion No. 228, June 11, 1952, Mimeo. ed. p. 24, where contentions similar to those made by Colorado were advanced, we held that production costs are so intimately associated with the volumes of gas produced that they are properly classified as commodity costs.

The staff classified transmission costs between demand and commodity based on behavior of cost studies and judgment. Supervision and engineering, and administrative and general expenses were classified between demand and commodity on the ratios developed from all other supervised expenditures, exclusive of compressor station fuel. Colorado assigned 100% of supervision and engineering to demand on the ground that such costs were dependent solely upon the size and location of the plant and had no relation to the volume of gas sold. Of administrative and

[25] Includes products extraction.

general expense, it assigned about 91.5% to demand and 8.5% to commodity, on the ground that most of such expenses do not vary with the volumes of gas transported and sold. Even if the salaries of officers of the company and supervisors are fixed, and even though all the time of such officials is not spent in direct contact with the employees of the company, we find that the only reasonable and equitable basis of spreading these costs is in proportion to the supervised expenditures. In this way, these costs are correlated in proportion to the dollar amounts of the supervised expenditures exclusive of compressor station fuel, which are made to carry on the business of the company and to earn revenues. And as we shall discuss in a moment, we do not adhere to the view that all fixed costs are ipso facto translated into the demand classification.

Compressor station labor, compressor station supplies and expenses (which includes compressor station fuel), and [fol. 118] maintenance of compressor station equipment were classified by the staff entirely to commodity. Colorado assigned compressor station labor 50% to demand and 50% to commodity; compressor station supplies and expenses, including compressor station fuel, 100% to commodity; and maintenance of compressor station equipment, 100% to commodity.

We have recently had occasion to review the problem of classifying costs for purpose of making a fair and equitable allocation of total costs between jurisdictional and non-jurisdictional business. Atlantic Seaboard Corporation, Op. No. 225, decided April 23, 1952; and Northern Natural Gas Company, Op. No. 228, decided June 11, 1952. We there held that all constant costs are not thereby translated into demand costs; that the determination of *how* much of the constant costs shall be apportioned between demand and commodity cannot be measured by the slide rule or mathematical formula; that such determination rests necessarily solely and entirely on judgment.

We found that in classifying compressor station labor, such costs partake of certain fixed characteristics, but both the capacity of a pipeline and its annual use are important cost incidences. We reach the same conclusion here. It

is our judgment that compressor station labor should be classified equally between demand and commodity. As to the other two items, compressor station supplies and expenses, including fuel, and maintenance of compressor station equipment, as to which there is no dispute between staff and Colorado in classifying such costs as 100% to commodity, we find that this is the proper classification for these two items.

"Other operating expenses" and "other maintenance expenses" were classified by the staff on the basis of 50% to demand and 50% to commodity. Colorado treats some of the items in these groups as 100% demand on the ground that after analysis of some of these items, Colorado's witness concluded such costs were fixed and therefore should be classified as demand costs. Even if we were to agree with the subsidiary facts, we are not necessarily bound to [fol. 119] reach the same conclusion that such items are fixed costs. For instance, Colorado's witnesses stated that the item "Other Operation Labor" represents the labor cost of operating dehydration plants. From this he reached the conclusion that such an expense was not related to the volume of gas transported. (T. 1674.) We reach a different and contrary conclusion. In our judgment we find such costs related to the volume of gas purchased and produced. Similarly Colorado's witness classified the cost labelled "transmission maps and records" as a demand cost—as not varying with the volumes of gas transported and sold.

But, whether we would or would not agree in every instance as to the few items analyzed by Colorado is not controlling with respect to the allocation of such constant costs. Colorado has treated all constant costs as demand costs, but this treatment assumes that classification of an item as a constant cost means that it is assignable 100% to demand. With this we cannot agree. As we stated in Atlantic Seaboard case, and repeated in the Northern Natural opinion,

"* * * A pipe line would not normally be built to supply peak service, that is to say, service on the peak days only. We know from our administration of Section 7 of the Natural Gas Act, which involves the issuance of certificates

of public convenience and necessity, that pipe lines are built to supply service not only on the few peak days but on all days throughout the year. In proving the economic feasibility of the project in certificate proceedings, reliance is placed upon the annual as well as the peak deliveries. Stated another way, the capital outlay for the pipe-line facility is made—and justified—not only for service on the peak days but for service throughout the year. Both capacity and annual use are important considerations in the conception of the project and the issuance of certificates of public convenience and necessity. Both capacity and volume, therefore, are what are known as cost factors or incidences in respect to the capital outlay for a pipeline project. It follows that reasonably accurate results can be achieved only by allocating the fixed expenses flowing from [fol. 120] the capital outlay to both operating functions, viz., capital and volume."

Thus, even if all such costs included in "Other Operating Expenses" and "Other Maintenance Expenses" are considered fixed, we find for these reasons and upon the record in this proceeding, that such cost should be classified 50% to demand and 50% to commodity. The staff has so treated these expenses and we adopt such classification.

The staff witness classified depreciation, taxes, and return equally between demand and commodity. Colorado classified all depreciation as a demand cost; other taxes except for state and federal income taxes and payroll taxes were classified as 100% demand. State and federal income taxes were classified 50-50, and return 50-50. We have referred in the Atlantic Seaboard and Northern Natural opinions to the fact that depreciation and return are related items. No useful purpose would be served in repeating here all that was said in those opinions. We find that there are no facts here warranting any departure from the principles announced by us on this matter. Demand and volume are important cost incidents in depreciation. We believe they should be given equal weighing in its classifications and we accordingly classify it 50-50. As to taxes, other than income taxes, we find that the property tax which is the largest item may be considered as a fixed cost and treated like depreciation and return.

Colorado classified income taxes and return 50-50. The reason given was that the cost of Colorado's funded debt was approximately 50% of Colorado's claimed 6½% rate of return and therefore 50% of the return was a fixed cost and the remainder was a variable cost. We find that return, like depreciation, is a fixed cost and because demand and commodity functions are important considerations, we shall classify return and income taxes (associated with the return) equally between demand and commodity.

[fol. 121] In transmission costs, there is included the costs for dehydrating the gas. The staff classified all dehydration costs, including taxes, depreciation and return, as 100% commodity on the ground that dehydration followed production and was directly proportional to the volume of gas processed. Colorado treated dehydration as it did its "other operating expenses." We find and conclude that dehydration costs are directly related to the volume of gas processed and should be classified 100% to commodity.

Distribution costs are less than two percent of the total cost of service. We find that the staff's method of classifying distribution costs 50% to commodity and 50% to customers on the basis of metering units is more reasonable and accurate than Colorado's demand-commodity classification.

In allocating the costs classified between demand and commodity, the staff allocated demand costs to classes of customers on the basis of the estimated normal peak day in 1952. Colorado estimated its 1952 revenues on the basis of a normal peak day. The staff has accepted such revenue estimates, and accordingly used the peak day on which Colorado estimated its revenue. Colorado allocated its demand costs on the basis of the actual system peak day sustained in the 1951-52 seasons; to-wit, February 24, 1952.

It was admitted by Colorado that all of the facilities, the costs of which are included in the cost of service studies of both staff and the company were not in service on February 24, 1952. Further, the revenue estimates were based on all these additional facilities being in operation. We conclude under the facts here, that the normal peak day for 1952 is the more reliable measure for allocating the demand costs.

As a practical matter the percentage of jurisdictional sales on the peak day used by the staff is 90% and non-jurisdictional is 10%. On Colorado's peak day the jurisdictional [fol. 122] is 90.39% and the non-jurisdictional is 9.61%, so that in effect the difference is de minimus.[26]

In allocating demand costs, the staff allocated such costs among the transmission pipeline customers. Colorado allocated its demand costs among all its customers, including sales made at the well mouth and in the field, on the ground that it classified production costs into demand and commodity. Since we have classified all production costs as commodity costs, it is only reasonable and proper that transmission line costs should be allocated to transmission line sales.

Colorado did not assign any of the Hugoton and Loveland field costs against its customer the Amarillo Oil Company. The staff pooled all production costs and spread such costs among all customers, including Amarillo Oil Company. Colorado excludes Amarillo Oil Company from all pooled production costs on the ground that Colorado, and its predecessor Canadian River, have a cost contract based on production in the Panhandle field. In spreading costs, all customers must share pro rata in the total costs. All customers, including Amarillo Oil Company, receive benefits from all the operations of the company. Amarillo Oil Company receives a benefit from Colorado's gas purchases in the Hugoton and Loveland fields to the extent that such purchases reduce the volumes which otherwise would be required to be produced by Colorado in the Panhandle field. We do not find that the cost contract between Colorado and Amarillo Oil Company is of such nature as to derogate from the general practice of pooling all costs and assigning them pro rata against all customers.[27]

In spreading its costs, Colorado has listed the sales to Colorado Springs, City of Trinidad and Public Service Company of Colorado for power plant use as a "direct

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[26] Excludes sales to Dalhart Gas Company.

[27] Re Northern Natural Gas Company, Opinion No. 228, page 40.

sale." At the time of the hearing, no sales were being made to the City of Trinidad for power plant use. Colorado admitted that the volumes it listed as sold to Colorado Springs as a direct sale were being sold under Rate Schedule I-1 on file with the Commission as a rate schedule covering sales for resale for industrial use. Additionally, [fols. 123-124] sales under the I-1 Rate Schedule are available only to those who purchase gas under the G-1 Rate Schedule, which is the sale for resale for general use. Colorado also admitted that the volumes it listed as a direct sale to Public Service Company for power plant uses were sold under Rate Schedule G-1, a rate schedule on file with the Commission covering sales for resale for domestic, commercial and industrial consumption. It estimated the amount to be used by Public Service in its power plant based on advice furnished to Colorado by Public Service in 1948. The staff considered all sales under the I-1 and G-1 Rate Schedules as sales for resale and therefore jurisdictional. Revenue estimates of sales to Public Service and Colorado Springs for boiler fuel use were based on rates in existing rate schedules. Colorado did not include such sales as jurisdictional. We conclude that on this record such sales should be included with the jurisdictional business.

There is nothing inconsistent here with Colorado Interstate Gas Company v. F. P. C., (C. A. 3), 185, F. 2d 357. That case simply decided that a rate schedule could be filed if stated in the terms of the statute that it was applicable only to sales for resale. Admittedly, all the sales to Colorado Springs and to Public Service Company are made pursuant to rate schedules on file with the Commission applicable to sales for resale.

The following tables show our findings and conclusions as to the classification of the cost of service and the allocation thereof among the various classes of customers.

(Here follows Table, folios 125-126)

[fols. 125-126]

TABLE No. 1

Colorado Interstate Gas Company
Excess Revenues and Cost of Service—By Functio
Year 1952

Line No.	(a)	Total (b)	Production: Hugoton and Loveland Fields Well Mouth (c)	Production: Hugoton and Loveland Fields Gathering (d)	Production: Panhandle Field Well Mouth (e)	Production: Panhandle Field Gathering (f)	Production: Hugoton Field Lakin (g)	Bi (h)
1	Gas Service Revenues	$17,962,532	$ ..	$ ..	$ ..	$ ..	$ ..	$.
	Cost of Service							
2	Operating Expenses	8,613,484	2,018,800	299,671	1,438,855	229,454	118,205	26
3	Depreciation	2,537,739	..	239,734	377,807	188,949	30,632	3
4	Depletion	57,688	..	..	57,688	..	..	.
	Taxes:							
5	Federal Income	185,599	848	16,899	25,455	10,590	2,231	
6	State Income	5,568	25	507	764	318	67	
7	Other	1,835,229	..	80,953	403,518	628,272	11,512	1
8	Return at 5¾%	3,280,317	14,989	298,689	449,888	187,175	39,442	3
9	Other Gas Revenues—Rent	(37,500)	..	..	..	..	..	(
10	Expense charged by Natural Gas Pipeline Co. of America to Fritch Operations	245,800	..	..	..	..	..	.
11	Sub-total	16,723,924	2,034,662	936,453	2,753,975	1,244,758	202,089	34
12	Allocation of Gasoline Plant Costs to Dehydration and Compression	..	..	..	..	..	..	(1
13	Sub-total	16,723,924	2,034,662	936,453	2,735,975	1,244,758	202,089	32
	Allocation of Costs to Gasoline:							
14	Bivins	..	..	..	(242,260)	(129,504)	..	20
15	Fourway	..	..	..	(106,916)	(56,741)	..	.
16	Fritch	..	..	..	(268,543)	(151,392)	..	.
17	Sub-total	16,723,924	2,034,662	936,453	2,136,256	907,121	202,089	53
18	Gasoline Revenues	(1,349,820)	..	..	..	..	(296,000)	(44
19	Sub-total	15,374,104	2,034,662	936,453	2,136,256	907,121	(93,911)	9
20	Loss on Gasoline Operations	(421,537)	..	..	..	..	..	(9
21	Cost of Service	$14,952,567	$2,034,662	$ 936,453	$2,136,256	$ 907,121	($ 93,911)	$.
22	Excess Revenues	$ 3,009,965						

88a

TABLE No. 1

Colorado Interstate Gas Company
ss Revenues and Cost of Service—By Functions
Year 1952

Line No.	(a)	Production Extraction Plants: nhandle Field uth Gathering (f)	Hugoton Field Lakin (g)	Panhandle Field Bivins (h)	Panhandle Field Fourway (i)	Fritch (j)	Extraction Costs Allocated to Dry Gas (k)	Transmission: Dehydration Panhandle Field (l)	Transmission: Other Transm. (m)	Distrbution (n)
1	Gas Service Revenues	$ ..	$ ..	$ ..	$ ..	$ ..	$ ..	$ ..	$ ..	$ ..
	Cost of Service									
2	Operating Expenses	855 229,454	118,205	262,127	146,620	93,100	..	44,236	3,721,478	240,938
3	Depreciation	807 188,949	30,632	36,556	50,290	..	..	17,485	1,573,054	23,232
4	Depletion	688 ..	..	..	..	..	..	..	..	..
	Taxes:									
5	Federal Income	455 10,590	2,231	2,017	3,961	..	..	1,383	120,361	1,854
6	State Income	764 318	67	61	119	..	..	41	3,611	55
7	Other	518 628,272	11,512	14,313	17,785	..	..	6,277	659,608	12,991
8	Return at 5¾%	888 187,175	39,442	35,647	70,908	..	..	24,431	2,127,270	32,778
9	Other Gas Revenues—Rent	..	..	(2,200)	(1,250)	..	..	..	(34,050)	..
10	Expense charged by Natural Gas Pipeline Co. of America to Fritch Operations	..	..	..	..	245,800	..	..	..	..
11	Sub-total	975 1,244,758	202,089	348,521	287,533	338,900	..	93,853	8,171,332	311,848
12	Allocation of Gasoline Plant Costs to Dehydration and Compression	..	..	(19,954)	(31,675)	(16,560)	..	50,208	17,981	..
13	Sub-total	975 1,244,758	202,089	328,567	255,858	322,340	..	144,061	8,189,313	311,848
	Allocation of Costs to Gasoline:									
14	Bivins	260) (129,504)	..	209,680	..	..	162,084	..	..	..
15	Fourway	916) (56,741)	..	..	55,250	..	108,407	..	..	..
16	Fritch	543) (151,392)	..	..	..	303,662	116,273	..	..	..
17	Sub-total	256 907,121	202,089	538,247	311,108	626,002	386,764	144,061	8,189,313	311,848
18	Gasoline Revenues	..	(296,000)	(446,500)	(228,500)	(378,820)	..	..	..	..
19	Sub-total	256 907,121	(93,911)	91,747	82,608	247,182	386,764	144,061	8,189,313	311,848
20	Loss on Gasoline Operations	..	..	(91,747)	(82,608)	(247,182)	..	..	..	..
21	Cost of Service	256 $ 907,121	($ 93,911)	$ ..	$ ..	$ ..	$ 386,764	$ 144,061	$8,189,313	$ 311,848

[fol. 127–128]

TABLE No. II

Colorado Interstate Gas Company
Summary—Allocation of Cost of Service
Total System
Year 1952

Line No.	(a)	Annual Volume Mcf[1] (b)	Revenue (c)	Cost of Service: Production (d)	Transmission (e)	Distribution[2] (f)	Total (g)	Excess Revenue Over Cost of Service (h)
	Transmission System Sales to Other Utilities							
1	Juridictional	86,119,000	$13,384,661	$3,278,988	$6,823,920	$ 170,566	$10,273,474	$3,111,187
2	Non-Jurisdictional	535,000	72,225	20,374	54,023	6,111	80,508	(8,283)
3	Total	86,654,000	13,456,886	3,299,362	6,877,943	176,667	10,353,982	3,102,904
4	Direct Sales	15,958,000	2,135,721	607,793	1,012,431	36,010	1,656,034	479,687
5	Total Transmission System	102,612,000	15,592,607	3,906,955	7,890,374	212,687	12,010,016	3,582,599
6	Leased Transmission System[3]	48,051,000	1,945,400	1,829,549	443,000	53,512	2,326,061	(380,661)
7	Field System	15,472,000	424,525	570,841	..	45,649	616,490	(191,965)
8	Total System	166,135,000	$17,962,532	$6,307,345	$8,333,374	$ 311,848	$14,952,567	$3,009,965

[1] Pressure base 14.65 p.s.i.a.
[2] Distribution Cost Classified 50% to Commodity & 50% to Customer.
[3] Sale to Natural Gas Pipeline Company of America.
() Indicates Red Figures.

(Here follows Table, folios 129-130)

[fol. 129–130]

TABLE No. III
Colorado Interstate Gas Company
Allocation of Cost of Service
Production System
Year 1952

Line No.		Well Mouth			Gathering		
		Volume Mcf[1]	Percent	Cost	Volume Mcf[1]	Percent	
	(a)	(b)	(c)	(d)	(e)	(f)	
	Transmission System Sales to Other Utilities						
1	Jurisdictional	86,119,999	51.837	$2,482,286	86,119,000	53.887	$
2	Non-Jurisdictional	535,000	0.322	15,419	535,000	0.335	
3	Total	86,654,000	52.159	2,497,705	86,654,000	54.222	
4	Direct Sales	15,958,000	9.605	459,949	15,958,000	9.986	
5	Total Transmission System	102,612,000	61.764	2,957,654	102,612,000	64.208	
6	Leased Transmission Facilities[2]	48,051,000	28.925	1,385,017	48,051,000	30.067	
	Field System						
7	Well Mouth	6,323,000	3.806	182,256	..	..	
8	Other	9,149,000	5.507	263,710	9,149,000	5.725	
9	Total Field	15,472,000	9.313	445,966	9,149,000	5.725	
10	Total System	166,135,000	100.000	$4,788,637	159,812,000	100.000	$

[1] Pressure Base 14.65 p.s.i.a.
[2] Sale to Natural Gas Pipeline Co. of America.
[3] Total of lines 14, 15, and 16, cols. (e) & (f) plus line 21, cols. (g) & (k).

TABLE No. III
Colorado Interstate Gas Company
Allocation of Cost of Service
Production System
Year 1952

Well Mouth			Gathering			Products Extraction			Total Production System
Volume Mcf[1] (b)	Percent (c)	Cost (d)	Volume Mcf[1] (e)	Percent (f)	Cost (g)	Volume Mcf[1] (h)	Percent (i)	Cost (j)	(k)
86,119,999	51.837	$2,482,286	86,119,000	53.887	$1,175,389	86,119,000	57.160	$(378,687)	$3,278,988
535,000	0.322	15,419	535,000	0.335	7,307	535,000	0.355	(2,352)	20,374
86,654,000	52.159	2,497,705	86,654,000	54.222	1,182,696	86,654,000	57.515	(381,039)	3,299,362
15,958,000	9.605	459,949	15,958,000	9.986	217,816	15,958.000	10.592	(70,172)	607,593
02,612,000	61.764	2,957,654	102,612,000	64.208	1,400,512	102,612,000	68.107	(451,211)	3,906,955
48,051,000	28.923	1,385,017	48,051,000	30.067	655,824	48,051,000	31.893	(211,292)	1,829,549
6,323,000	3.806	182,256	..	..	..	..	..	..	182,256
9,149,000	5.507	263,710	9,149,000	5.725	124,875	..	..	..	388,585
15,472,000	9.313	445,966	9,149,000	5.725	124,875	..	..	..	570,841
66,135,000	100.000	$4,788,637	159,812,000	100.000	$2,181,211	150,663,000	100.000	$(662,503)[2]	$6,307,345

(g) & (k).

[fol. 131–132]

TABLE NO. IV

Colorado Interstate Gas Company
Allocation of Cost of Service
Transmission System
Year 1952

Line No.	(a)	Annual Sales Volumes MCF[1] (b)	Normal Peak Day Volume MCF[1] (c)	Demand Percent (d)	Demand Amount (e)	Commodity Percent (f)	Commodity Amount (g)	Leased Facilities (h)	Total (i)
	Transmission System								
	Sales to Other Utilities								
1	Jurisdictional	86,119,000	363,427	90.036	$2,973,677	83.927	$3,850,243	$ ..	$6,823,920
2	Non-Jurisdictional	535,000	3,680	0.912	30,121	0.521	23,902	..	54,023
3	Total	86,654,000	367,107	90.948	3,003,798	84.448	3,874,145	..	6,877,943
4	Direct Sales	15,958,000	36,536	9.052	298,966	15.552	713,465	..	1,012,431
5	Total Transmission System	102,612,000	403,643	100.000	3,302,764	100.000	4,587,610	..	7,890,374
6	Leased Transmission System[2]	48,051,000	..	..	..	..	..	443,000	443,000
7	Total Transmission	150,663,000	403,643	100.000	$3,302,764	100.000	$4,587,610	$443,000	$8,333,374

[1] Pressure Base 14.65 p.s.i.a.
[2] Sale to Natural Gas Pipe Line Company of America.

TABLE No. IV

Colorado Interstate Gas Company
Cost Classification
Transmission System
Year 1952

Line No.	Particulars	Transmission			Cost Classification		
		Dehydration	Other	Total	Demand	Commodity	Other
	(a)	(b)	(c)	(d)	(e)	(f)	(g)
	Operations						
1	Supervision & Engineering	$ ..	$ 77,974	$ 77,974	$ 31,579	$ 46,395	$ ..
2	Compressor Station—Fuel	..	195,900	195,900	..	195,900	..
9	Compressor Station—S & E	..	253,104	253,104	..	253,104	..
4	Other Operating Expenses	..	1,080,423	1,080,423	540,211	540,212	..
5	Total Operations	.	1,607,401	1,607,401	571,790	1,035,611	..
	Maintenance						
6	Supervision & Engineering	..	71,329	71,329	18,546	52,783	..
7	Compressor Station Equipt	..	358,424	358,424	..	358,424	..
8	Other Maintenance Expense	..	379,739	379,739	189,869	189,870	..
9	Total Maintenance	..	809,492	809,492	208,415	601,077	..
	Miscellaneous						
10	Rents	..	2,497	2,497	1,248	1,249	..
11	Rental of Leased Facilities	..	443,000	443,000	..	..	443,000
12	Total Miscellaneous	..	445,497	445,497	1,248	1,249	443,000
13	Dehydration	44,236	..	44,236	..	44,236	..
14	Administrative and General	..	859,088	859,088	296,385	562,703	..
15	Depreciation	17,485	1,573,054	1,590,539	786,527	804,012	..
16	Other Gas Revenues—Credit	..	(34,050)	(34,050)	(17,025)	(17,025)	..
17	Taxes—Federal Income	1,383	120,361	121,744	60,180	61,564	..
18	Taxes—State Income	41	3,611	3,652	1,805	1,847	..
19	Taxes—Other	6,277	659,608	665,885	329,804	336,081	..
20	Return @ 5¾%	24,431	2,127,270	2,151,701	1,063,635	1,088,066	..
21	Costs Allocated to Dehydration	50,208	17,981	68,189	..	68,189	..
22	Total Cost of Service	$144,061	$8,189,313	$8,333,374	$3,302,764	$4,587,610	$443,000

( ) Denotes Red Figures.

[fol. 135-136]

TABLE NO. V

Colorado Interstate Gas Company
Allocation of Cost of Service
Distribution System
Year 1952

Line No.	(a)	Sales Volumes Mcf[1] (b)	Percent (c)	Commodity Cost (d)	Metering Units Number (e)	Percent (f)	Customer Cost (g)	Total Distribution Cost (h)
	Transmission System							
	Sales to Other Utilities							
1	Jurisdictional	86,119,000	51.837	$ 80,826	64.0	57.554	$ 89,740	$170,566
2	Non-Jurisdictional	535,000	0.322	502	4.0	3.597	5,609	6,111
3	Total	86,654,000	52.159	81,328	68.0	61.151	95,349	176,677
4	Direct Sales	15,958,000	9.605	14,977	15.0	13.489	21,033	36,010
5	Total Transmission System	102,612,000	61.764	96,305	83.0	74.640	116,382	212,687
6	Leased Transmission Facilities[2]	48,051,000	28.923	45,098	6.0	5.396	8,414	53,512
7	Field System	15,472,000	9.313	14,521	22.2	19.964	31,128	45,649
8	Total System	166,135,000	100.000	$155,924	111.2	100.00	$155,924	$311,848

[1] Pressure Base 14.65 p.s.i.a.
[2] Sale to Natural Gas Pipeline Company of America.

[fol. 137] Utilizing the Demand and Commodity costs herein allocated to Sales to Other Utilities—Jurisdictional and the billing units applicable to such sales, we obtain the following rate structure:

Rate Schedules G-1 and G-2
Demand Charge: 81¢ per Mcf
Commodity Charge: 8.5¢ per Mcf
Rate Schedule G-1 adopted by Colorado from Canadian River
14.5¢ per Mcf
Rate Schedule P-1
17.5¢ per thousand cubic feet for the first 5 days' use of the billing demand
8.5¢ per thousand cubic feet for all additional gas
Rate Schedule I-1 (not including that adopted by Colorado)
11¢ per Mcf
Rate Schedule I-2 (including Rate Schedule I-1 adopted by Colorado)
9¢ per Mcf

Such rate structure, which we find to be just and reasonable will result in revenues for the test year of $10,289,269, as compared with the allocated cost of service of $10,273,474 for gas estimated to be sold under the above rate schedules in 1952.

The allocation of the cost of service indicates that the existing rate for sales to Natural Gas Pipeline Company does not cover the cost of service for that sale. The sale to Natural Gas Pipeline Company is made pursuant to Rate Schedule S-2, applicable only to that sale. Estimated revenues under the existing rate do not meet the cost of service for this sale by $380,661. We have already held that under Section 5(a) of the Natural Gas Act we are not permitted to order an increase in the rates to one customer in a rate proceeding, even though the effect of our order is to produce lesser total overall revenues. Atlantic Seaboard Corporation, Op. No. 225, page 40. We shall require by order that Colorado shall file rate schedules which shall effect the reduction heretofore found to be due to customers other [fol. 138] than Natural Gas Pipeline Company.

For the same reason we can not increase the rate applicable to Clayton Gas Company from the present rate of 14.5¢ per Mcf to the rate being prescribed herein for Rate Schedule G-1. Furthermore, the rate being prescribed in Rate Schedule G-2 for the City of Trinidad sale is the same as that being established for Rate Schedule G-1, thus continuing the present rate pattern. While service to Trinidad is not at city-gate, but at the end of a buyer-owned lateral, we cannot say on this record to what extent this factor should be taken into account. No issue with respect thereto was raised at the hearing.

Insofar as the sales to Natural Gas Pipeline Company and Clayton Gas Company are concerned Colorado will have to take the initiative under Section 4 of the Act in proposing rates which are not unjust, unreasonable, unduly discriminatory or preferential.

On November 2, 1951, Colorado filed a motion for a finding that the staff had failed to meet the burden of proof on the ground that staff's presentation up to the time of the filing of the motion consisted of evidence based on the operations of the Company for the year ending June 30, 1951, which did not include the additional facilities proposed to be placed in operation during 1952. Thereafter, both the staff and the company introduced evidence on the company's operations for 1952 including the additional facilities. Indeed, the year 1952 has been used as the test year. It is appropriate therefore to deny Colorado's motion.

On November 15, 1951, Colorado filed a second motion for a finding that staff had failed to sustain the burden of proof. Colorado reserved the right to cross-examine staff's witnesses and introduce its own evidence. By order of November 30, 1951, we reserved decision on the motion until the matter was before us for final decision. In view of our findings heretofore made, and our order thereon, it is appropriate to deny this motion filed by Colorado.

[fol. 139] The Commission further finds:

(1) The rates and charges made, demanded and received by Colorado Interstate Gas Company for or in connection with its transportation and sale of natural gas subject to the jurisdiction of the commission under its Rate Sched-

ules G-1, G-2, P-1, I-1, and I-2, as they appear in its FPC Gas Tariff, Original Volume No. 1, and under Rate Schedules G-1 and I-1, as they appear in the FPC Gas Tariff, Original Volume No. 1 of Canadian River Gas Company, which Colorado has adopted, are unjust, unreasonable and excessive in the sum of $3,111,187 based upon the test year 1952.

(2) The rates and charges of Colorado Interstate Gas Company for or in connection with its transportation and sale of natural gas subject to the jurisdiction of the Commission described in (1) above after reflecting a reduction of $3,111,187 as hereinafter provided and ordered will be just and reasonable.

The Commission orders:

(A) The rates and charges made, demanded, or received by Colorado Interstate Gas Company for or in connection with its transportation and sale of natural gas in interstate commerce for resale for ultimate public consumption under its Rate Schedules G-1, G-2, P-1, I-1, and I-2, as they appear in its FPC Gas Tariff, Original Volume No. 1, and under Rate Schedules G-1 and I-1, as they appear in the FPC Gas Tariff, Original Volume No. 1 of Canadian River Gas Company, which Colorado has adopted, shall be so reduced as to reflect a reduction of not less than $3,111,187 based upon the test year 1952.

(B) Colorado Interstate Gas Company shall file on or before September 15, 1952, the following schedules of rates and charges for or in connection with its transportation and sale of natural gas in interstate commerce for resale for ultimate public consumption, which new schedules of rates and charges shall be effective as to deliveries and sales from and after the date of issuance hereof:

[fols. 140-141] Rate Schedules G-1 and G-2

Demand Charge: 81¢ per Mcf
Commodity Charge: 8.5¢ per Mcf

Rate Schedule G-1 adopted by Colorado from Canadian River
14.5¢ per Mcf

Rate Schedule P-1

17.5¢ per thousand cubic feet for the first 5 days' use of the billing demand

8.5¢ per thousand cubic feet for all additional gas

Rate Schedule I-1 (not including that adopted by Colorado)

11¢ per Mcf

Rate Schedule I-2 (including Rate Schedule I-1 adopted by Colorado)

9¢ per Mcf

(C) The motions to dismiss filed by Colorado Interstate Gas Company on November 2 and November 15, 1951 be and the same are hereby denied.

By the Commission.

Leon M. Fuquay, Secretary.

Date of Issuance: August 8, 1952.

* * * * * * *

[fols. 142-146] BEFORE THE FEDERAL POWER COMMISSION

* * * * * * *

PETITION FOR REHEARING, VACATION AND MODIFICATION—

Filed August —, ——

Comes now Colorado Interstate Gas Company (hereinafter called Colorado) and presents this its petition and application for rehearing and modification of the order of the Commission issued in the above matter on August 8, 1952 ordering decreases in the rates of Colorado and prescribing rates to be observed, as well as denying motions to dismiss and for findings that due notice required by law had not been granted to Colorado. The rehearing herein applied for is made upon each and all of the errors, objections and grounds set forth in the following Specifications of Errors, Grounds for Vacation and Modification and Grounds Relied Upon. Each matter set forth in said Speci-

fications of Errors and Grounds Relied Upon constitutes objection and exception to the order of the Commission and the Commission erred in every such respect.

A. Specification of Errors

* * * * * * *

[fol. 147] 16. The Commission erred in concluding that a fair rate of return to Colorado would be 5¾% and that such return is "adequate to assure confidence in the financial soundness of the utility; to maintain its credit and to enable it to attract capital necessary for the proper discharge of its public duties" (p. 42)*; and in failing to find

17. The Commission erred in concluding in respect of rate of return that said rate of 5¾% will enable Colorado to attract future new capital, whereas the most recent costs in the record in this case in respect of debt money are 3¾% while the Commission used the average historical cost of debt money of 3.21%, and the Commission further erred in respect thereof in concluding "that appropriate adjustments of rates can be made when experience demonstrates that adjustment is required" (p. 37).

[fol. 148] 18. The Commission erred in concluding as to the cost of equity capital entering into rate of return that purchasers of Colorado stock recently purchased said stock based on an earnings-offering price ratio of 7.03% with earnings-net price to the selling stockholders of 7.44%.

19. The Commission erred in fixing the rate of return solely upon its concept of the bare historical cost of money without allowing over and above the bare cost of money such amount as in its judgment would be proper to attract capital in the future, all as required by applicable law upon this subject.

20. The Commission erred in concluding that Colorado would experience a loss in gasoline operations since it has presumed to follow a theory which is not based upon the substantial evidence of record, which is based upon data

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* Unless otherwise indicated, page references in parenthesis will refer to the mimeographed opinion of the Commission in the above matter issued August 8, 1952.

that the minimum rate of return should be 6½%.

missing from the record, and which is contrary to all of the substantial evidence of this record.

21. The Commission erred in making the following conclusion (p. 44):

"Westpan in turn, sells the finished gasoline, and after deducting ¼th cent per gallon as cost of marketing, remits 50% of the gross revenues to Colorado."

22. The Commission erred in asserting as follows (pp. 45-46):

"The Staff allocated the joint wellmouth and gathering costs on the basis of the relative market value theory of joint production, a method generally employed in the petroleum industry. Under this method the joint costs are apportioned to the finished product on the basis of the relative market values of such products. The direct costs incurred to make each product fully marketable are deducted from the respective market values of the finished products so as to determine relative market values at the point of processing where joint operations cease."

23. The Commission erred in finding (p. 46):

"The five cent value of the dry gas was based on the then [fol. 149] latest reports of the Texas Railroad Commission as to the weighted average market price at the wellhead paid for gas being used and sold in the Panhandle field. The report of September 12, 1951, based on evidence submitted at a hearing before that Commission states that the Texas Railroad Commission finds that the weighted average wellhead price being paid in the Panhandle Field is 4.8526 cents per M.c.f. measured on a 16.4 pressure base. Further, Colorado or its predecessor, Canadian River, paid the Texas production tax based on the market value of its gas at 4.33 cents per Mcf. The staff assigned all the costs of the gasoline plants to the gasoline operation, except such costs as applied to the steam and cooling facilities to dehydrate the gas entering Colorado's transmission line."

24. In determining the cost of producing, gathering and processing said liquid hydrocarbons, the Commission erred in the following respects:

(a) In failing to find that there is no evidence in this record as to the proper allocation factors to be used in the

application of the relative market value theory of cost allocation.

(b) In finding that the relative market value method as applied by the Staff produces a result more reasonable than Colorado's method and in presuming to apply the relative market value theory of cost allocation in the absence of evidence in this record as to the factors to be used in making an allocation under such method.

(c) In failing to consider that, assuming for the purposes of this Specification of Error only that the relative value factors were present and the method were a valid one, the circumstances of a wide fluctuation of the value of natural gasoline as opposed to the fixed character of the dry gas price renders the relative market value method valueless and inappropriate in this case.

(d) In failing to recognize that the relative market value method of assuming to determine costs does not in fact de- [fol. 150] termine costs and is used only as an expedient when used at all.

(e) In using the relative market value method for the purpose of allocating joint costs with factors of value which have no relation to reality and in fact are contrary to all of the substantial evidence of record, particularly, to wit, that the value attributed to the dry gas is only 50% of the true value as set forth in this record.

(f) In failing to recognize that authorities agree that the volumetric method of allocation is the preferable one.

25. After concluding that neither the relative market value method nor the volumetric method is entirely satisfactory, the Commission erred by failing to open the record for the purpose of having its Staff or some responsible person introduce such evidence as would in the minds of the Commission provide a method for properly determining and allocating gasoline costs.

26. The Commission erred in determining that the fairness of the method used for the allocation of joint gasoline costs was to be determined from results rather than from an allocation method based upon reality which would produce fair results.

27. The Commission erred in costing gasoline operations by setting forth the conclusion it desired to be reached and

in the light thereof deciding which of the supposed allocation methods in this record it would adopt.

28. In not doing what it purported to do in respect of costing the gasoline plant operations, to wit, the application of the relative market value method as applied by the Staff, the Commission erred as follows: The Commission has allocated wellmouth and gathering costs to gasoline in the amount of $1,116,059 in contrast to wellmouth and gathering costs allocated to gasoline by the Staff in the amount of $715,340.

29. The Commission erred in making its determination [fol. 151] and allocation of costs of the gasoline operations by presuming to follow a method and then failing so to do.

30. The Commission erred in concluding as follows (p. 56):

"Thus, of the total wellmouth and gathering cost, $2,805,920 is allocated to dry gas and $1,116,059 to natural gasoline. The joint gasoline plant costs are allocated $386,764 to dry gas and $150,435 to natural gasoline. The gasoline plant costs directly assigned to natural gasoline amount to $208,863. The total cost therefore applicable to the production, gathering and processing of the liquid hydrocarbons owned by Westpan into finished gasoline is $1,475,357. The total revenue accruing to Colorado under the merger agreement for gasoline operations is estimated by it for 1952 to be $1,053,820. Therefore, from such operations there is a net loss or excess of cost over revenues of $421,537. Under the terms of the certificate which we issued to Colorado in Docket No. G-1326, supra, page 48, which terms and conditions were accepted by Colorado, this loss is not to be considered as *as* cost of service to Colorado Interstate's natural gas customers and consumers. Accordingly, we find and conclude that the loss of $421,537 shall not be considered as a part of the cost of service which we have heretofore determined."

31. The Commission erred in adopting, as stated by it, one of two unsatisfactory methods of costing the gasoline operations and in applying any result obtained by such method, assuming only for the purposes of this Stipulation of Error that such method was properly applied and pre-

sented, since the requirement of the Commission's order in Docket G-1326 allows the adjustment assumed to be made only after determination of "the costs properly allocable to such hydrocarbons."

32. The Commission erred in not setting forth in its opinion the evidence and bases upon which it arrives at its factors for the determination and allocation of costs of the gasoline operations, and in not setting forth such findings, facts, and detail as would enable Colorado or any reviewing court to determine the bases upon which the Commission proceeded in making its determinations in re- [fol. 152] spect of the allocation of joint costs, nor can it be determined what weight the Commission gave to the evidence on this subject, and the Commission erred in not setting forth that information.

33. The Commission erred in the adoption of a 5¢ value for dry gas in each and every one of the particulars set forth below, to wit:

(a) The Commission erred in determining (p. 46): "The 5 cent value for the dry gas was based on the then latest reports of the Texas Railroad Commission as to the weighted average market price at the wellhead paid for gas being used and sold in the Panhandle Field."

(b) The Commission erred in assuming and stating that Colorado's predecessor paid the Texas production tax based in the market value of its gas at 4.33¢ per M.c.f.

(c) Assuming for the purpose of this Specification of Error only that the determinations of the Texas Railroad Commission give a proper value factor, the Commission erred in using a so-called valuation at the end of 1950, whereas the test year purported to be used by the Commission is 1952.

(d) The Commission erred in attributing a so-called valuation of dry gas to Colorado which was based upon patently incomplete data as to its predecessor constituent, Canadian River Gas Company.

(e) The Commission erred in adopting 5¢ as the value of dry gas based on reports of the Texas Railroad Commission since reference thereto (Exh. 2) will show clearly that the Canadian River Gas Company values were based on royalties paid by it, and the order herein shows (p. 23 et

seq.) that royalties are now paid by Colorado on the basis of 8¢ at the wellhead; and the Commission further erred, therefor, in not attributing to the dry gas for allocating gasoline costs this latest determination of value assuming for the purpose of this Specification of Error only that the Commission is justified in using the relative market value theory.

[fol. 153] 34. The Commission erred in ignoring or failing to evaluate all the evidence relating to costing gasoline operations which evidence would show that only the volumetric method is related to the facts of this case.

35. The Commission erred in not weighing the evidence and in not determining that the only substantial evidence indicates that the volume of natural gasoline and dry gas in a common stream governs the size and capacity of wellmouth and gathering facilities.

36. The Commission erred in not finding that the Staff did not satisfy its burden of proof in that it failed to produce a satisfactory method of allocating costs to gasoline.

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40. The Commission erred in not allowing to Colorado Federal Income Taxes and State Income Taxes, associated with the 5¾ per cent rate of return found by the Commission to be reasonable and, in fact the Commission has reduced the allowed rate of return from 5¾ per cent to 5.01 per cent.

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[fol. 154] 47. The Commission erred in failing to find that the end result of the proposals of the Staff is unfair, [fols. 155-156] unjust, unrealistic and amounts to confiscation of property of Colorado.

48. The Commission erred in failing to find that the cost of needed supplies of gas to Colorado is greatly in excess of the commodity price allowed to be charged by Colorado to its customers.

49. The Commission erred in using a cost basis for determining the allowable wellmouth costs for gas produced in the Panhandle Field included in the cost of service and in failing to use the value thereof since the end result thereof is unjust, unreasonable, and discriminatory in that

the said treatment of the Commission allows to Colorado's royalty owners in the Panhandle Field over 3.16 times the amount Colorado realizes from the production operation.

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[fols. 157-158] 53. The Commission erred in failing to grant a rehearing of its order issued May 26, 1952 wherein it ordered the omission of the intermediate decision procedure in this case and in refusing to vacate said order as requested in said application for rehearing.

54. The Commission erred in failing to find that this proceeding involved one which is accusatory in nature and in which issues of fact were sharply contraverted and that, therefore, the decision of the Presiding Examiner was required in order to grant to Colorado a fair hearing.

55. The Commission erred in concluding in its order issued May 26, 1952 that "due and timely execution of its functions imperatively and unavoidably requires the Commission to omit the intermediate decision procedure in this proceeding."

56. The Commission erred in not recognizing that there was no substantial evidence upon which to base the finding set forth in the immediately preceding Specification of Error.

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[fols. 159-166] C. Grounds Relied Upon

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[fol. 167] VIII

Specifications of Errors Nos. 16, 17, 18 and 19

In arriving at the amount of 5¾% as a reasonable rate of return the Commission has used the historical cost of money to Colorado. The effect of the use of this historical cost is to limit the return of Colorado not to a present cost of money but to what it actually has paid in the past for its money assuming that the Commission has arrived at a correct determination on the cost of equity. This clearly does not comport with the legal requirement in respect to rate of return since it is required thereby that the

return should be reasonably sufficient to assure confidence and financial soundness, support credit and enable the Company to raise the money necessary for the proper discharge of its duties. The bare bones cost of money allows nothing for the future attraction of capital. The Commission has recognized this when it holds that its activities in rate matters are a continuing process and that if the Company incurs increased costs for money it may seek relief from the Commission. This is relief after the fact, which comprehends the necessary regulatory lag. The Commission by its own rationale therefore has confirmed the fact that there is missing here that extra fillip which would attract money in the future. The Commission in effect says therefore that since this fillip is missing it will make it up after the fact. Such ex post facto relief withheld from the rate of return clearly does not accord with the judicial standards mentioned above. In speaking of a rate of return large enough to attract capital the Supreme Court of the United States was not talking of what a future rate of return might be but of what a present rate of return must be (Bluefield Water Works, an improvement company, vs. Public Service Commission, 262 U. S. 679 (1922); Federal [fol. 168] Power Commission vs. Hope Natural Gas Company, 320 U. S. 591 (1944)). The Commission moreover did not even allow the present cost of debt money but instead used the historical rate of 3.21%.

The Commission also errs in respect of the equity portion of the rate of return by concluding that the recent marketing of Colorado's stock was equivalent to financing on a 7.44% earnings net price to the selling stockholders. Analysis of the record in this case will show that this conclusion is unfounded. Since there is no appreciable difference between the Staff and Colorado on rate base it is obvious that the rate of return is a crucial factor. Total rate base approximates $57,200,000 (Exh. 26). Since $31,600,000 (Exh. 43) is represented by debt and preferred stock there remains $25,600,000 attributable to common stock and surplus. The Commission asserts that 8.45% (p. 41) return on equity is adequate to attract new capital and seek to support this argument by pointing to the recent marketing of 966,000 shares of Colorado's common stock on April

2, 1952 (Exh. 43). The net received by the selling stockholders (which from the Commission's treatment presumably would be the net that Colorado would receive) was $25.25 per share (Exh. 43). Pro forma 1951 earnings were $1.88 per share (Exh. 43). This the Commission asserts is equivalent to financing on a 7.44% basis and therefore the Commission assumes that allowing the Company 8.45% return on equity would be adequate.

The fallacy of the above reasoning is that the stock could not be sold on 8.45% return on rate base equity. The book value of the stock is $13.63 as found by the Commission and the $1.88 per share represents 13.79% rate of return. It is this book value which the Commission in effect uses in computing rate of return. By applying this 8.45% to rate base equity in the amount of $25,600,000 the earnings of $2,163,200 would be $1.26 per share. The record discloses that the market price of natural gas transmission companies stocks were anywhere from 1½ to 2½ times their book value. (In fact one stock sells at 4 times the book value.) (Tr. pp. 1076-1077.) Therefore a 9% rate of return on rate base equity is the equivalent of a 3.6% to 6% [fol. 169] rate of return on current market prices. It is apparent that a strict application of the Commission's formula in this case would mean that the average natural gas transmission company would have to pay about twice as much for equity financing as has been the case in the past.

IX

Specifications of Errors Nos. 20, 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, 32, 33, 34, 35 and 36

The Commission in its adoption of one of the two methods of costing gasoline which it held to be unsatisfactory has purported to adopt the relative market value method proposed by the Staff. Attending for the moment to the record in this case in regard to such method, analysis will indicate that the fundamental principle of the method is missing. The Staff witness by assuming to use the relative market value method to use prices reflecting the current value attached to the products. He did not do this,

however, but instead, took all of the prices paid for natural gas in the West Panhandle Field of Texas even though this weighted average method resulted from contracts negotiated twenty years or more ago (Tr. pp. 1283-1287). The Staff witness admits that this is not "market Price" but, instead, market price is the price between a willing buyer and a willing seller in a competitive market in recent transactions and the transactions have to be recent (Tr. pp. 1293-1294). This admission from the only witness testifying in support of the relative market value or market price method has the effect of taking from his method one of the factors making up the ratio from which costs under his method are to be determined. The witness did not use the market value or market price method but has used something else. There is no evidence, therefore, to support the use of the method which the Commission purports to use.

As support for the use of 5¢ value for dry gas, the Staff witness and the Commission both use reports of the Texas Railroad Commission (Exhs. 1 and 3). No matter what the Texas Railroad Commission or Colorado or its predecessor, [fol. 170] Canadian River Gas Company, used for the computation of the Texas production tax, the base determined by the Texas Railroad Commission simply is not the market value of the gas. This is apparent from the exhibit itself since this determination is based upon averages of prices stemming from ancient as well as recent transactions. The determination of costs by a relative market value or price ratio comprehends nothing but the use of current prices. To deviate from the method is to repudiate the method. Therefore, the only evidence in this record upon which the Commission could act was that submitted on behalf of Colorado as to the costing of gasoline plant operations.

Even if the Staff witness had used the proper ingredients of his assumed method, the Commission has perverted it and has acted without any evidence in the allocation of wellmouth and gathering costs. This is evident from the fact that the Commission in purporting to use the method of the Staff upon the same facts determined higher costs as being applicable to the wellmouth and gathering operations. Analysis will disclose that what the Commission

has done has been to determine a new ratio for the division of costs by considering what is done inside of the gasoline extraction plant and relating the percentages so determined clear back through gathering and wellmouth facilities. This simply cannot be done because all evidence of record indicates clearly that there are two great divisions of operations involved with different costs, different values and different factors involved after the cessation of wellmouth and gathering operations and before the actual extraction process within the gasoline plant. The Commission, therefore, acted without evidence in the premises.

The Commission failed to evaluate and weigh the evidence in regard to the market value method of costing joint products. The Commission has failed to weigh the evidence indicating that the relative market value method does not measure costs but merely divides them (Exh. 42).

The only evidence of record as to the current market value of gas in the Panhandle Field is 10¢ per M.c.f. and not the 5¢ used by the Staff (Tr. pp. 1484-1485). By the [fol. 171] use of this true market value factor, revenues accruing to Colorado would exceed costs in the gasoline plant operations even by the use of the relative market value method of dividing costs. This conclusion is supported by the only evidence in the record as to what the real market value of gas is (Exh. 41). The bald assertion of the Commission that the relative market value method of costing joint products is a method generally employed in the petroleum industry fails to take into consideration the undisputed evidence that where this method is used it is used as an expedient and it is agreed by the experts that it is second in desirability to the volumetric method (Tr. p. 1488). The only reference of record on the subject indicates clearly that the volumetric method is the only one comporting with the facts. This is particularly true of the important items of cost entering into the category of wellmouth and gathering costs, for the facilities of a gas well and gathering lines necessary for the transportation of the combined stream of natural gasoline and dry gas as wet gas are determined by the volume of this combined product (Tr. p. 1418). There is no other

evidence in the record to refute this considered opinion of two expert engineers well qualified on the subject. In fact, the same record supports the proposition that volume determines the cost of the installations within the extraction plant. The Commission apparently would avoid this problem by noting that under the merger arrangement Westpan Hydrocarbon Company may require Colorado to install additional extraction facilities. The Commission does not point out, however, that no such requirement has yet been made, may never be made and, in any event, the criterion of prudent operations marks the top liability of Colorado (Item O).

The Commission here under the justification of the condition in its order in the merger case has assumed to attribute costs to gasoline operations. The merger case condition required Colorado to absorb costs in excess of revenues accruing to it, but as the order in that case expressly recites it is only "the costs properly allocable to such hydrocarbons" which are to be considered in imposing such liability. The Commission cannot determine the costs prop- [fol. 172] erly allocable to the hydrocarbons without having before it a thoroughly satisfactory method of cost determination. The Staff, therefore, failed in its burden of proof in this regard and there is no substantial evidence upon which the Commission could act.

The Commission, since it has assumed to use the evidence of the Staff regarding the 5¢ value for dry gas, was completely in error when it stated (p. 46) that the 5¢ value was based on the latest reports of the Texas Railroad Commission. The evidence shows clearly that the Staff witness on this problem knew of a higher later published price of the Texas Railroad Commission but did not use it (Tr. pp. 1281-1282). Therefore, the Commission's conclusion is clearly contrary to the evidence.

The statements of the Commission that Colorado's predecessor (Canadian River Gas Company) paid the Texas production tax on a 4.33¢ M. c. f. market value is wrong. Reference to the taxing statute will show that market value is not the criterion for payment in this case since said statute provides:

"The market value of gas produced in this State shall be the value thereof at the mouth of the well, however, in case gas is sold for cash only, the tax shall be computed on the producer's gross cash receipts "(Vernon's Annotated Revised Civil Statutes of the State of Texas, Tit. 122, Art. 7047(b)(2)).

Since Canadian River Gas Company, and now Colorado, sells its gas for cash only, not market value but what is received for the gas on a regulated and old contract basis determines the tax, therefore, the Commission acted with complete disregard of the statute and without the essential factor for its ratio in determining costs under its assumed method.

The dry gas price of Colorado is fixed but the gasoline price fluctuates widely, this fact, authorities agree, renders the relative market value method valueless. The Staff witness, however, was not affected by this defect in his approach (Tr. pp. 384-386).

[fol. 173] In any event the price assumed to be used by the Commission was based at best upon data applicable only for the last six months of the year 1950 (Exh. 2). If the Commission is using 1952 as a test period, it must, therefore, use an indicia of value relating to 1952. It has not done so. The value should be the actual current market value under the relative market value method. The only evidence in this record indicates that the value of gas in the Panhandle Field approximates 10¢ per M. c. f. The Staff has not shown any value of gas beyond 1950, therefore, for the Commission to adopt as a valuation factor this antiquated data constitutes acting without substantial evidence.

Regardless of what else the Commission has done, it also, by the use of the Texas Railroad Commission determinations, has acted without complete data as to almost 2/5ths of the total production of gas involved. This is made abundantly clear from Exhibit 2 wherein the Texas Railroad Commission indicates that it had data in respect to approximately 33 billion cubic feet of Colorado's predecessor's production but no information as to 20½ billion thereof.

If it is assumed that it was proper for the Commission to use data such as the old published reports of the Texas Railroad Commission, which Colorado denies, the Commission did not arrive at a proper value determination since reference to Exhibit 2 will show that the Texas Railroad Commission determination is based upon royalties as to Colorado's predecessor. The Commission in its opinion and order in this case, however, recognized that royalties have increased so that royalty payments are based upon a participation in gas to a valuation of 8¢ (pp. 23-24). The Commission, therefore, has been arbitrary and inconsistent and has acted contrary to the substantial evidence and its own findings in failing to use as the dry gas factor in its valuation the value of natural gas based upon 8¢ per M. c. f. at the wellhead. The effect of the use of such ratio with this changed factor as found by the Commission would be materially to reduce, if not entirely eliminate, the gasoline costs which the Commission determined were not chargeable to the rate payer.

[fols. 174-175] The Commission also has mistakenly used the 5¢ value purportedly based on determinations of the Texas Railroad Commission. The Texas Commission's determinations are at the wellhead whereas the 5¢ value used by the Commission is at the point of split-off in the gasoline plant. Between the wellhead and split-off point the gathering and processing increase the value of the gas. The Commission shows in its opinion (Table I, Line 13, Col. f) gathering costs of $1,244,758 for gathering and (p. 55) $386,764 of joint gasoline plant processing costs applicable to gas at the split-off point. Therefore, there is no evidence that the value of the gas at the wellhead found by the Railroad Commission is the value at the split-off point.

The Commission's determination regarding the costing of gasoline plant operations is defective and such pervades the Commission's whole opinion and order inasmuch as there is not contained therein or in the record in this case such information as is required to understand how the Commission arrived at its determining figures for making the allocation of costs attributable to gasoline appearing at page 55 of the opinion. Specifically, there is required the

details of determination of Joint Well Mouth and Gathering Costs for each gasoline plant and for all plants shown on line 2 of the table on page 55. Also, there are required the details for determining Joint Gas and Gasoline Costs, Direct Gasoline Costs, and Direct Dry Gas Costs for Bivins and Fourway Gasoline Plants shown under note 1 on page 55.

The volumetric method is the only appropriate method here since (i) it accords with the facts—volume determines side of facilities; (ii) it accords with the Commission's method of allocating other costs; and (iii) this is the only method supported by the qualified expert witnesses in this case (Tr. pp. 1417-1418).

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[fol. 176] XI

Specification of Error No. 4

The Commission in its treatment of the cost of service because of the deduction for the alleged loss on gasoline plant operations has de-rived Colorado of the rate of return to which it is entitled. Under the regulatory concept a utility is to be allowed Federal income taxes which it would pay on a fair return. The Commission clearly has recognized this when it recently stated:

"It has been our consistent practice to allow in the Cost of Service, the amount of Federal income taxes which the utility would actually pay to the Government based upon a fair return, adjusted for all tax credits to which the corporation is entitled." (Mimeo. Opinion No. 227, In re Transcontinental Gas Pipe Line Corporation, Docket No. G-1842, p. 30).

In the present case the Commission did not do this as will be demonstrated below. If the loss on gasoline operations were not treated by the Commission as a tax deduction, which it clearly is not, (no more than would be the disallowed cost of the new fees to be paid to directors and members of the Executive Committee), the following would

[fol. 177] reflect the income tax calculation based upon the return:

Return at 5¾%		$3,280,317
Deduct:		
Interest	$ 964,300	
Amortization and Sundry	12,025	976,325
Sub-total		$2,303,992
Tax Adjustments:		
Depreciation per Cost of Service	$2,537,739	
Depletion per Cost of Service	57,688	
Total	$2,595,427	
Statutory Depreciation	$2,327,417	
Statutory Depletion	1,356,251	
Intangible Drilling Costs	585,920	
Cost of Removal	26,395	
Total	$4,295,983	
Net Tax Deductions		1,700,556
Sub-total		$ 603,436
Surtax Allowance ($25,000 × 22%)		5,500
		$ 597,936
Taxable Income ($597,936 ÷ 48%)		1,245,700
Tax at 52%		647,764
Less Surtax Allowance		5,500
Federal Income Tax		$ 642,264

This tax, assuming all other determinations of the Commission to be correct, is properly calculated. The Commission, however, allowed only $185,599 as tax. The action of the Commission in this regard, therefore, is arbitrary,

capricious, discriminatory and highly prejudicial to Colorado.

* * * * * * *

[fol. 178] XII

Specifications of Errors 43, 44, 45, 46, 47 and 48

The Commission erred in failing to realize that the end result of its rate determination and the end result of all of the proposals made by the Staff is inherently unreasonable and no rate reduction should be made on such basis. This record clearly shows that at present Colorado is having to pay more for its gas in order to keep currently abreast of the demands upon its system than the 8.5¢ allowed by the Commission as a commodity charge under the General Service Rate Schedules(Tr. pp. 727, 1484). The Commission by its order issued in Docket G-1677 (Item N) has found that there is a deficiency of the supply on the part [fol. 179] of Colorado and the conclusions of the Commission implicitly require Colorado constantly to increase its available supply of natural gas. It is inherently unreasonable and confiscatory, therefore, to set rates at a city gate on a basis which is less than the cost which Colorado has incurred and will have to incur in the field in order to acquire such additional supplies.

XIV

Specification of Error 49

The end result of the Commission's order is obviously unjust and unreasonable when one makes comparison of the amount of money accruing to Colorado as return upon the basis determined by the Commission . It is well recognized that the greatest of risks inhere in the activities of a producer of oil or gas. The result, however, of the Commission's determination in this case is not to compensate Colorado for these risks but rather to prejudice it therein. Analysis of the result of the Commission's order will show that Colorado's royalty owners, who do nothing but receive their royalties, are compensated more than three times more for the production activity necessarily required than is Colorado. This is evident from the following analysis:

Analysis of Panhandle Field Well Mouth Costs Found Reasonable by the Commission in Opinion 235

Item	Total Cost	Unit Cost Per Mcf Sold
(1)	(2)	(3)
Gas Royalties	$1,422,730	1.02¢
All Other Operating Expenses	16,125	.01
Total Operating Expenses	$1,438,885	1.03¢
Depreciation	$ 377,807	0.27¢
Depletion	57,688	0.04
Federal Income Taxes	25,455	0.22
State Income Taxes	764	
Other Taxes	403,518	0.29
Return @ 5¾%	449,888	0.32
Total of Above	$2,753,975	1.97¢
[fol. 180]		
Less Portion of Above Costs Allocated to Gasoline	617,719	0.44
Net Well Mouth Cost Allocated to Gas	$2,136,356	1.53¢

Note: Figures in Column (2) are from Opinion 235, Table I and pp. 23-24. Figures in Column (3) are derived by driving costs in Column (2) by sales of 139,430,000 Mcf which is the volume of gas produced in Panhandle Field and sold to customers by Colorado Interstate (Exh. 37, Sched. 14).

Since the Commission adds to the production activity only costs of transportation, distribution, etc., it is obvious that Colorado is being dealt with discriminatorily when its compensation for the production of gas is restricted as above indicated. This is a most graphic portrayal of an unjust end result. The unit cost per M.c.f. of the gas sold at the well is 1.53¢. This, in the face of the prices shown in this record, and of which the Commission has official knowledge, indicates clearly the need for a new approach to the problem.

XVI

Specifications of Errors 53, 54, 55, 56, 57, 58, 60, 61, 62 and 63

The Commission omitted the intermediate decision procedure over the objection of Colorado and by inaction is deemed to have denied Colorado's petition for rehearing

filed in respect of such omission. This proceeding was defi- [fol. 181] itely accusatory in nature as the Commission was advised in the answer and in the petition for rehearing filed by Colorado in this matter. That the issues were sharply controverted also is so demonstrated, and the Commission's opinion indicates this fact. For the Commission so to act and omit the intermediate decision procedure in this case was therefore a violation of the Administrative Procedure Act (Section 8), the requirements of due process of law and amounted to a denial to Colorado of that fair hearing to which it is entitled. While Section 8 of the Administrative Procedure Act empowers an administrative agency to omit the intermediate decision, it still requires the finding "upon the record that due and timely execution of its functions imperatively and unavoidably so requires." Bearing in mind that this investigation of the Commission began September 2, 1948 and was not brought to hearing until October 1, 1951, the finding of the Commission that it had to omit the intermediate decision is made without any substance or evidence whatsoever.

The Commission has not and could not demonstrate that the timely execution of its functions "unavoidably" required it to take this case from the Presiding Examiner. The Commission's first obligation is to accord to Colorado a fair hearing. That a fair hearing may require more time than an unfair hearing is no reason for granting only an unfair hearing. The effect of what the Commission has done has been to deny to Colorado that appraisal of the credibility of witnesses and the weight to be given to their evidence which only the presiding officer could have given. There can be no excuse for the Commission's action other than undue haste to dispose of a case. Thus there has been taken from Colorado a part of the record in this all-important controversy to which Colorado is entitled and which a court may consider in determining whether the Commission's ultimate findings are based upon substantial evidence.

The facts of this case indicate unfairness toward Colorado also in that the action of the Commission was taken after all briefs had been filed. In a case as involved as a rate proceeding is, the great and detailed analyses are

made in briefs. But the brief submitted to a trial examiner [fol. 182] is pitched to a different plane than that which is submitted to a body which has not heard the evidence. Therefore, Colorado in effect has been denied its right to brief the questions involved. The Commission allotted to Colorado only 60 minutes of time in which to present orally its contentions. The circumstances clearly indicate that such time is not adequate in which to detail all of the matters involved in this rate proceeding and this grant of an oral argument cannot be considered as an acceptable substitute for the right to brief the question or argue the same in full. Therefore the Commission has effectively thwarted Colorado's right to a fair hearing and its conclusions, therefore, are not in accordance with the requirements of due process of law and cannot stand.

Aside from the general requirement of due process of law that reasonable notice must be given, the Administrative Procedure Act in Section 4 requires notice which, by the legislative history of the Act, is to be such notice as could fairly appraise Colorado of the issues involved so that it may present relative data or argument (see report of the House Judiciary Committee, Administrative Procedure Act, Legislative History, Senate Document No. 248, 79th Congress 2d Sess., p. 258). Colorado assiduously tried in this case to learn from the Staff of the Commission what claims were being made. The record clearly indicates that the Staff constantly refused to give such notice (Tr. pp. 330, 1085, 1143-1146, 1180-1187, 1205-1206). In fact, it was not until Staff counsel filed his first brief, at which time Colorado also had to file a brief contemporaneously with that of Staff counsel, that it was indicated that Staff counsel was depending for the claims made against Colorado upon the test period of 1952 as set out in Exhibit 26. This the Commission refers to as Staff rebuttal. Therefore, in its principal brief Colorado was unable yet to know what assertions and claims were being made by the Staff against it. This is an obvious denial of reasonable notice any *and* findings, conclusions or orders of the Commission made in pursuance of such proceedings cannot stand. Furthermore the Staff in so acting has acted outside of the pale of fair play, due process of law and thereby has failed to sustain

[fols. 183-187] any proof or proffer any proof upon which the Commission may act.

XVII

Specification of Error No. 59

Both under the Administrative Procedure Act (Section 7) and the Commission's Rules of Practice and Procedure (Section 1.27) the Presiding Examiner is in control of the proceeding and his actions in the matter of recessing hearings and other procedural steps are not subject to interference with this Commission in the absence of arbitrary action. Therefore, the action of the Commission in interfering with a recess declared by the Presiding Examiner after weighing all relevant facts (Tr. pp. 1217-1229) constituted a denial to Colorado of its right to a fair hearing particularly inasmuch as the Commission's interference occurred midway in the recess period found by the Examiner to be required.

* * * * * * *

[fol. 188] BEFORE THE FEDERAL POWER COMMISSION

OPINION NO. 235-A AND ORDER ON APPLICATION FOR REHEARING—Issued September 29, ——

Before Commissioners: Thomas C. Buchanan, Chairman; Dale E. Doty, Claude L. Draper and Harrington Wimberly.

September 26, 1952.

Application for rehearing and motion for stay of our Opinion No. 235 and Order issued on August 8, 1952, in the above-docketed proceeding, were filed by Colorado Interstate Gas Company (Colorado) on August 27, 1952.

Numerous specifications of errors are advanced by Colorado. None require rehearing, although one of them warrants minor modification of the opinion and order respecting the industrial rate schedule applicable to Clayton Gas Company. Our order establishes a rate of 9¢ per Mcf for sales of industrial gas to Clayton as compared to the prior rate of 9.5¢ per Mcf. This reduction is inconsistent with

our finding that Colorado's rates for service to Clayton are below the cost of service. Accordingly, we will modify our order issued August 8, 1952 to retain the 9.5¢ per Mcf rate in Rate Schedule I-1 for firm industrial service to Clayton. [fol. 189] Colorado complains that we did not indicate in our opinion and order which of the data we considered for 1952, the test year. This complaint is frivolous for the data upon which we based the rate reduction are explicitly set forth. Thus, the table on page 4 of the opinion (mimeo. copy) shows the components involved in the rate-making process as claimed by the Staff and Colorado, and the differences between them. These data, underlying our decision, are fully discussed in the balance of the opinion and order.

In this connection, we note that Colorado is concerned regarding our description in the opinion of certain evidence offered by the Staff and by Colorado as "rebuttal" evidence. It is Colorado's concern that such reference shows that we may not have accorded such evidence the consideration to which it is entitled. Our description, however, is directed to the point of time or order in which the evidence was introduced at the hearing. Our decision regarding the weight of that evidence and the inferences, findings and conclusions to be drawn from the evidence were not influenced by or dependent on the order in which the evidence came into the record. All of the evidence received in the record, whether introduced as part of the case-in-chief, rebuttal, or sur-rebuttal has been fully considered. Indeed, we allow as part of Colorado's expenses, amounts claimed by Colorado in what we may properly call its "sur-rebuttal" case.

Colorado also challenges our consideration of federal income tax accruals as available for working capital purposes. Our determinations in this case disclosed that there were available to Colorado for working capital purposes tax accruals of $139,199.00. We, therefore, found that the working capital requirement which should be included in the rate base should be offset by that amount. Colorado does not, in its application for rehearing, challenge the propriety of off-setting tax accruals against working capital requirements. Its contention is only that it had no

notice during the hearings that tax accruals would be so treated and that it has, therefore, been deprived of due [fol. 190] process of law, and that this deprivation amounts to confiscation of its property.

It is an accepted practice in computing the rate base on which the utility is entitled to earn a fair return to include an amount representing the utility's working capital requirements. This is done on the theory that the funds required for such purpose are contributed by the investors and, therefore, are in the same category as funds contributed by investors for the construction of utility plant which is devoted to the customer's service.

From this it is obvious, of course, that in any computation of the working capital requirements it is appropriate to take into account funds contributed by the customers which are available for working capital purposes and which diminish the amount required to be made available by the investors for such purposes. In the case of Colorado, it is not open to question that Colorado's customers contribute, through rates, amounts which are intended to enable Colorado to meet its federal income tax liabilities. These funds are contributed by the customers in advance, often far in advance, of the time when they must be paid over by Colorado to the Federal Government. It is not open to question that such amounts are available for working capital purposes and do not represent funds contributed by the investors upon which the utility is entitled to earn a return.

We do not believe that any deprivation of procedural due process is involved. The computation of a proper working capital allowance was one of the issues in the case as to which Colorado had full notice and the availability of tax accruals for such purposes was equally well known to Colorado.

The exclusion from the rate base of $139,199 only affects Colorado's return by $8,003.94 representing 5¾% return on $139,199. Not only is this amount of $8,003.94 de minimis, but under the rate we have ordered to be placed in effect, there will be an excess of $15,795 in revenues over cost of service (p. 74 of the opinion), which amount easily absorbs the $8,003.94. We find, therefore, that rehearing

is not required with respect to the working capital determination.

[fol. 191] Colorado attacks our allowance of a 5.75% rate of return contending that:

(1) We did not allow present cost of debt capital but, instead, used an historical rate of 3.21%;

(2) We did not allow that extra "fillip" as Colorado puts it which is necessary to attract money in the future; and

(3) In determining the reasonable cost of common stock capital we erred in applying earnings-price ratios in relation to the book value of the common stock.

As to the first contention, it is true that 3.21% cost of debt capital was historically incurred in the sense that Colorado's Serial Notes were issued in the past. It is completely erroneous, however, to state that we did not allow the present cost of that capital. Actually, Colorado's present cost of debt capital is 3.21%. Interest and other costs associated with debt capital naturally continue in respect to that part of the capital represented by the debt until such debt is redeemed or is retired. There can be no question whatsoever that the present cost of debt capital is 3.21% and this we fully recognized.

There are no facts of record which show what the rate of debt money will be at some unknown time in the future when the company may raise additional debt capital. As a matter of fact, there is nothing in the record which shows that the company has either definite or indefinite plans to raise additional debt capital. The use of a higher rate of interest than that which is presently being paid by the company would, therefore, merely represent and unwarranted additional allowance for the common stock equity and would not represent proper cost of debt capital.

As to the allowance of an extra "fillip," such allowance was not made in respect to debt capital because of the absence of any showing that such an extra allowance was even remotely appropriate. We did, however, make an allowance over and above the percentage of returns on common stock which are currently reflected in the purchase of natural gas company securities. Thus it was shown that

[fol. 192] investors have been buying common stocks since 1945 on the basis of approximately 8.3% earnings. In other words, the earnings which appear to be available to natural gas common stocks when related to the purchase price of those stocks by investors indicate that investors have been requiring on the average an earning of 8.3%. As of October 1, 1951 the stock of representative natural gas companies was being bought on the open market on the basis of 6.4% earnings. Moreover, a large block of the stock of Colorado Interstate Gas Company was sold in April 1952 in the face of a pending rate reduction proceeding on the basis of 7.03% earnings as measured by relating earnings to the market price of the stock. Our rate of return of 5.75% when broken down by capital elements, results in an 8.45% return on the common equity after an allowance of ½% for the cost of floating the stock. Accordingly, we allowed more than the "bare bones" cost of capital.

Colorado contends that, in measuring the return required by investors, we misapplied the percentage relationship of the earnings available to common stock to the market value of common stock that is, the earnings-price ratio. Colorado argues that if the earning-price ratio is used it should be applied to the market value base for the stock instead of the book value. Such an application would have the effect of departing from the investment rate base and substituting, in part, a fair value base according to the proportion of common stock to other capital of the company.

In the alternative, Colorado contends that the 8.45% earnings-price ratio should be applied to the actual investment in such manner as to effect a 13.79% return on the common equity. This contention is as novel as it is lacking in merit. It too would require the rate of return to be fixed so as to maintain the market value of the stock. This is circular reasoning. It is well known that the chief factor affecting the market value of a common stock is the earnings of a corporation. Accordingly, inasmuch as market [fol 193] value reflects the earnings position, the allowance of earnings sufficient to maintain that market value would completely defeat effective regulation. Excess earnings would result in excess market value which, under the

theory, must be maintained; inadequate earnings which would result in a depressed market value would likewise have to be maintained if all that is required under the principle stated is the maintenance of the market value of the stock. Under this scheme, if high earnings are once obtained they could never be reduced through rate regulation, whereas inadequate earnings could not be increased. The plan is entirely devoid of merit. Market values of securities are the result and not the cause of earnings. A fundamental error would be committed in the determination of a fair rate of return if it were fixed with a view of maintaining the market value of securities.

Evidently there is misunderstanding by Colorado as to the Commission's weighing of earning-price ratios and yields on common stocks in determining the over-all rate of return. It has long been recognized that the best means of determining what investors require in the way of return as to all classes of capital, debt, preferred stock, and common stock, is by resort to the prices prevailing on the securities markets. If a corporation has 4% bonds outstanding and such bonds are selling at a premium so as to yield 3%, that is good evidence that the return required of such a bond by investors is 3%. By the same token, if investors are investing large sums of money in common stock on the basis that their return, expressed in earnings, will amount to 8% and yield 5½% to 6%, that is good evidence of how the investors appraise the common stock in relation to other investment opportunities and is likewise good evidence as to the return required by investors to attract their capital.

The significant factors, therefore, the *the* relationships of earnings to price paid by investors and dividends to price. These relationships disclose the investor's appraisal of the securities under consideration and, as stated above, what the investors require in the way of return. The market value of the stock is not here important per se but is [fol. 194] only important in showing the percentage return which investors will insist upon to be attracted to the enterprise.

It is not possible, on this record at least, nor is it in any way necessary, for us to determine a reasonable rate of

return for Colorado a long time in the future. The return may be affected by many events such as the amount and interest rate of debt securities issued, the additional stock, preferred or common, floated, and the ratio of the capital items to the total capital structure. It is not at all unlikely that the issuance of additional debt capital, even at a higher rate than 3.21%, would result in a lower over-all cost of money because of the change in the capital structure whereby a larger percentage thereof would be represented by low-cost capital items. It will be appropriate to consider these matters when their occurrence is a fact or at least is shown to be imminent.

Accordingly, we affirm our determination that a 5.75% rate of return in this case is just and reasonable.

Colorado contends we erred in several respects in our use of the relative market value method for allocating between dry gas and natural gasoline the joint production, gathering and processing costs. It is alleged that there is no evidence to support the use by us of such method. Such allegation appears to be negated by the extended discussion by Colorado of the evidence dealing with this subject. Other than its expressed preference for the volumetric method which we have already considered and rejected as producing an unreasonable result, Colorado's chief criticism centers upon our use of a 5¢ per Mcf market price for dry gas.

Colorado seems to believe that the relative market value method is invalid unless the current market prices of the respective products are used. We do not agree, for in our judgment it would not be proper to use the spot market prices of either dry gas or natural gasoline for allocating joint costs, and we have, therefore, used average market prices both for dry gas and gasoline. Colorado finds no fault with our use of the average market price for gasoline but maintains that the true market value factor which we should use for the dry gas is the current market value of [fol. 195] 10¢ per Mcf alleged to prevail in the Panhandle field. The evidence relied on by Colorado, in our judgment, does not require alteration of the 5¢ per Mcf price. That evidence consists of testimony by a witness for Colorado that he had seen a contract for the purchase of gas

in the West Panhandle field by Panhandle Eastern Pipe Line from Shell Oil and Sinclair Oil dated August 30, 1951, providing for a price of 9.5¢ per Mcf at a 16.4 pound pressure base. Moreover, the contract prices of natural gas in other fields which are in the record could only be recognized if data of probative value relative to the market prices of natural gas in the Panhandle field were lacking. This is not the case.

The Texas Railroad Commission is required by law[1] to determine annually or semiannually the market price being paid at the wellhead for natural gas to be used or sold in the Panhandle field for light and fuel purposes. The record contains two reports of the Texas Railroad Commission wherein there are set forth data with respect to market prices being paid at the wellhead for gas used and sold for light and fuel purposes. In the report (Exhibit No. 3), dated January 10, 1951, there are set forth various contract prices paid for gas at the wellhead under contracts made during the period commencing July 1, 1948, and extending through October 31, 1950, as well as prices paid under contracts between various pipe-line companies. In the second report (Exhibit No. 2), dated September 12, 1951, the weighted average market price was found to be 4.8526¢ per Mcf (16.4 psi). The earlier report does not purport to cover prices paid on a field-wide basis such as does the latter report, of September 12, but reflects only prices paid under the contracts made during the period indicated. Such wellhead contracts specify prices ranging from a low of 3.12655¢ per Mcf to a high of 5.36¢ per Mcf, the arithmetical average being 4.37059¢ per Mcf. The report of [fol. 196] September 12 also contains a comparison of the weighted average prices for various periods running from 1942 through 1950. These data show that over this period there has been a gradual but steady increase in the weighted average prices paid for gas at the wellhead in the Texas Panhandle field. The weighted average price on a 16.4 pressure base was 4.1005¢ per Mcf in 1942. During

[1] Senate Bill No. 227, amending Section 3 of Article 6008a, Title 102, Vernon's Annotated Civil Statutes of the State of Texas, Subdivision (f).

the intervening years the prices increased gradually to 4.8526¢ in the last half of 1950.

Colorado makes reference to the fact that there is a higher later published price of the Texas Railroad Commission which was not considered. The evidence shows, however, that such later report does not require a revision in the 5¢ per Mcf we have used.

Colorado also claims that we were wrong in stating that Colorado's predecessor (Canadian River) paid the Texas production tax on a 4.33¢ per Mcf market value and cites the applicable provision of the Texas statute which reads as follows:

"The market value of gas produced in this State shall be the value thereof at the mouth of the well, however, in case gas is sold for cash only the tax shall be computed on the producers gross cash receipts." [2]

Colorado contends that, since it (and its predecessor) sold gas for cash, only, it cannot be said that the production tax was based on the market value. We think Colorado has misread the statute since the cash sale referred to must obviously be at the wellmouth. The record does not show that the Texas production tax is computed by Colorado on the basis of the cash received by it for the gas sold in its market areas but rather it is computed upon the basis of a declared market value. The declaration by Colorado of a market value of 4.33¢ per Mcf as the basis for computing its production tax is only one of the indicia of the market price of gas in the Panhandle field which we may and did properly take into consideration. Our conclusion would [fol. 197] not be altered even if we disregarded Colorado's payments pursuant to this statute.

Colorado maintains that since the market price determinations by the Texas Railroad Commission are wellhead prices whereas the 5¢ per Mcf price used by us is at the point of split-off in the gasoline plant, the cost of gathering and processing should be added since that increased the value of the gas. We were well aware of this fact and

[2] Vernon's Annotated Revised Civil Statutes of the State of Texas Tit. 122, Art. 7047b(2).

gave consideration thereto in determining the 5¢ price used in the allocation. We also took into consideration the fact that the wellhead price determined by the Texas Commission is for wet gas and that the gas after extraction of the liquid hydrocarbons would have a lesser value. The evidence shows the value of the gasoline content of the gas at the split-off point is approximately 2¢ for each Mcf of wet gas processed.

In our determination of an appropriate market price to be used for the dry gas at the point of split-off in the gasoline plant we took all of these factors into account. It is our view that the 5¢ per Mcf price is reasonable, based upon the evidence, and may be appropriately used for the purpose of allocating the joint production, gathering and processing costs between dry gas and natural gasoline.

Colorado complains that we have not included in our opinion full details as to how we arrived at the determining figures for making the allocation of costs attributable to gasoline appearing at page 55 of the opinion (mimeo. copy). We think our opinion contains sufficient details for Colorado to verify from the record the basic data which we used and to ascertain precisely how our determinations were made. Nevertheless we annex hereto as part of this opinion and order Tables I and II containing appropriate record reference which will facilitate Colorado in determining the details which it states it requires.

Colorado alleges that it has been deprived of the rate of [fol. 198] return to which it is entitled by reason of our treatment of the loss on gasoline operations in computing income taxes. Colorado claims the federal income tax allowance is properly calculated at $642,264, whereas our allowance is $185,599, or a difference of $456,665.

The difference between the claimed income tax liability and the income tax allowance we provided is the result of our treatment of the loss on gasoline operations of $421,537. We have found that the loss on gasoline operations should not be considered a part of the cost of service and with this finding Colorado does not take issue. Colorado would have us compute its federal and state income tax liabilities on the basis of earnings which do not reflect a reduction in the cost of service of the $421,537. To accede to Colorado's

contention, however, is to nullify the removal of the $421,537 from the costs which the customers of Colorado should bear. For under Colorado's claim the $421,537 denied it, as recovery of a loss on gasoline operations would be recovered in substantial part from the customers in the guise of a reimbursement for a higher tax liability only part of which would in fact be incurred.

Colorado alleges that the Commission by its order changed the character of service of Rate Schedule I-1 as contained in the tariff of Canadian River Gas Company, applicable to the sale of industrial service gas to Clayton Gas Company from "firm service to service subject to curtailment and having a priority below that which Clayton had enjoyed." Of course, we did nothing of the sort. In the case of all rate schedules referred to at pages 74 and 79 of the opinion, we specified the rates to be included in the rate schedules required to be filed by Colorado Interstate. No change in any existing service classification was ordered, and none was contemplated or inferred.

Colorado objects to the omission of the intermediate decision procedure. In our order of May 23, 1952, omitting that procedure, we stated the subsidiary facts on which we made our finding that "due and timely execution of our functions imperatively and unavoidably required" the omission in this proceeding. We adhere to the view expressed [fol. 199] there that these subsidiary facts are sufficiently substantial to warrant and support the requisite statutory finding. We have had occasion recently to note the increased number and magnitude of formal proceedings now pending before us, particularly rate proceedings under the Natural Gas Act, and that this increase has created a growing burden on our limited staff, including examiners, necessitating unavoidable delay in the disposition of these matters before this Commission.[3] These factors, while no

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[3] Mississippi River Fuel Corporation, Docket No. G-1641, order of June 3, 1952; Alabama-Tennessee Natural Gas Company, Opinion No. 226-A, June 10, 1952.

necessary to our decision to omit the intermediate decision procedure in this case, cannot be overlooked in any consideration of the matter.

Finally, we note that Colorado filed a motion for stay of our rate reduction order on August 27, 1952, and thereafter, on September 8, 1952, while the motion and its application for rehearing were still pending, sought and secured a stay of our order and an injunction from the United States Court of Appeals for the Tenth Circuit. We have moved to vacate the stay and injunction on the ground, inter alia, that the court was without jurisdiction until Colorado has exhausted its administrative remedies and filed a petition for review in the court. However, we are faced with the fact that a stay and injunction have issued which deprive the Commission of its discretion respecting Colorado's motion for stay, rendering inappropriate any action on that motion at this time.

The Commission further finds:

(1) Opinion No. 235 and order, issued August 8, 1952, should be modified as hereinafter ordered.

(2) No new facts have been presented or alleged in Colorado Interstate Gas Company's application for rehearing and no principles of law are stated in the application, which either were not fully considered by the Commission before it entered Opinion No. 235 and order issued August 8, 1952, or which, having now been considered, warrant further hearing, modification except as hereinafter ordered, [fol. 200] or abrogation of the opinion and order.

The Commission orders:

(A) The following, appearing on page 74 of the opinion (mimeo. copy):

"Rate Schedule 1-2 (including Rate Schedule 1-1 adopted by Colorado)
9¢ per Mcf"

be modified to read as follows:

"Rate Schedule 1-2
9¢ per Mcf
Rate Schedule 1-1 (adopted by Colorado)
9.5¢ per Mcf"

(B) The following, appearing in paragraph (B) of the order issued August 8, 1952:

"Rate Schedule I-2 (including Rate Schedule I-1 adopted by Colorado)
9¢ per Mcf"

be modified to read as follows:

"Rate Schedule I-2
9¢ per Mcf
Rate Schedule I-1 (adopted by Colorado)
9.5¢ per Mcf

(C) The petition for rehearing be and the same is hereby denied.

(D) The effective date of this Opinion No. 235-A and Order is September 26, 1952.

By the Commission. Commissioner Draper not participating. Commissioner Wimberly concurs in the findings and order.

Leon M. Fuquay, Secretary.

Date of Issuance: September 29, 1952.

(Here follows Table I, Table II, folios 201, 202, 203, 204)

thing else, when right here we are faced with the bald proposition of law, and I maintain I am willing to submit the staff's case on the question of law that Your Honor has raised. We have not included the new facilities, and we are perfectly willing to let the Commission determine rates which we say as a matter of law the Commission can determine for the future without including those new facilities. I think that is simple enough.

* * * * * * *

Mr. McGee: We appreciate the consideration you have given to our request, Mr. Examiner.

Whereupon, at 2:40 p. m., the hearing was recessed, to reconvene at 10:00 o'clock a. m., November 6, 1951.

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Mr. Goldberg: Mr. Examiner, on November 2, 1951 Colorado Interstate Gas Company and Canadian River Gas Company, the companies involved in this rate proceeding, filed two motions: One, a motion for a finding that the Staff has failed to meet the burden of proof; and two, a motion for continuance pending the disposition of the motion for a finding that the Staff had failed to sustain the burden of proof.

The motion for a finding that the Staff has failed to meet the burden of proof is grounded on the fact that Staff's case is based on the actual experience of these two companies on a pro forma merged basis for the 12 months ending June 30, 1951 and does not take into consideration the operations of the merged company resulting from au- [fol. 212] thorized future expansion.

There is nothing in this record to show when these added facilities will go into operation, nor is there anything in this record to show how the omission of these new facilities will affect the net revenues of the merged company.

Further, when Staff prepared its direct testimony, it appeared that the additional facilities would not go into operation in the immediitate future.

It is still our view that as a matter of law, based on the facts and circumstances as disclosed on this record to date, the Commission may legally fix the rates in this proceeding for the future based on the record as it now stands.

However, because we now understand for the first time that some of these facilities are expected to go into operation during the current month, and in order to expedite these proceedings and avoid further delay by any present arguments on the motion filed by these companies that Staff has failed to meet the burden of proof, the Staff requests the opportunity to adduce evidence with respect to these future expansions.

In view of the fact that the two motions hereinbefore mentioned were filed only last Friday, although the hearing was recessed a month ago, the Staff requests that it be granted two days' time—in other words, to Thursday, November 8, 1951—to prepare such additional evidence.

To this extent it joins in the request for continuance filed by the companies.

If this request to adduce additional evidence is granted, it is submitted that the motion for a finding that the Staff has failed to sustain the burden then becomes moot.

Presiding Examiner: Do you gentlemen wish to make any statement?

Mr. White: Mr. Examiner, I think in the interests of [fol. 213] orderly procedure, that the request of the Staff should be denied.

They have put in their case in chief and the record to that extent, as I conceive of it, is closed.

I do not know how many shots they are supposed to have at this particular piece of game, but it appears to me that when they closed their case, they have put in what we should consider to be the best case which under the circumstances they could offer and, if that case is defective as a matter of law, I think we are entitled to a ruling on that point.

I would vigorously oppose any reopening of the Staff's direct case, or in effect what I imagine it would amount to would be putting in a new direct case, and in effect the Staff would be asking that the previous direct evidence put in by it be ignored.

Now, if that is the situation, it seems to me that we might go on here for years and years, with everybody putting in cases in chief all the time and, consequently, we would always have to open up our right again to investigate that and put in our own answer to it.

It seems to me that, as I said in the beginning of my remarks, they have had their opportunity to present the best case they could present. I think the presumption is that that is what they have done and, if that is defective as a matter of law, I believe that we are entitled to a ruling on it, sir.

So far as the time element is concerned, it appears to me that, in view of the pendency of the motion to in effect dismiss this proceeding because of insufficiency as a matter of law in the evidence, that the continuance should be granted for that to such a period of time as all parties in interest might have an opportunity to answer under the rules and, consequently, it would be more or less a waste of time and effort to proceed this morning with the cross-examination of the Staff's witnesses when in the end the result might be that the case would be thrown out anyway.

Presiding Examiner: As the Examiner stated earlier, [fol. 214] the period for cross-examination was fixed in the light of the existing record and the nature of the material; that is, the nature of the material, weighing the elements that were new as against the elements that were simply book figures. We made a very careful analysis of that.

The Staff's request—in fact, there are two requests, as I understand it, Mr. Goldberg: One is that you be permitted to supplement your direct case.

Mr. Goldberg: Yes, sir.

Presiding Examiner: It seems to me that before ruling on the matter of continuance, the Examiner should consider that request, and I think the record well should show the things that appear to the Examiner that are pertinent to that ruling.

There has been no cross-examination on the case. Therefore, all that has been said is that we have finished. The Staff now, before there is any cross-examination, indicates that they desire to supplement their direct testimony.

It seems to me that, while in the courts that is discretionary, nevertheless where there is indication that the new testimony relates itself to new facts, that the court would certainly be remiss not to permit a party to supplement their direct case, and I think that is the situation before the Examiner.

It seems to me there could be no possible harm. After all, the purpose of these hearings is in order that the Commission may have all of the facts that bear upon the performance of their statutory duty.

It seems to me, therefore, I am compelled to grant the motion to reopen and supplement the direct case.

The Staff says they only need two days. That certainly is not such a delay as would adversely affect anybody, and it seems to me that the only thing for the Examiner to do, therefore, is to grant the motion for continuance for two days.

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[fol. 215] Mr. White: Mr. Examiner, I think it is appropriate to point out at this time that the exhibits which have been introduced in evidence this morning on behalf of the staff contain data, some of them, in respect of three different years, 1951, 1952, 1953. Both Exhibit 13 of Mr. Wiskup and Exhibit 18 of Mr. French purport to show cost of service and purport to show some type of allocation for all of those three years.

Now, it appears to me, sir, that we are entitled here to reasonable notice of the claims which are going to be made

[fols. 201-202]

TABLE I

Determination of Joint Well Mouth and Gathering Costs
Year 1952

	Overall Costs			Gasoline Plants			
	Amount	Mcf at 16.4 p.s.i.a.	Cents per Mcf	All Plants	Bivins	Fourway	Fritch
Gas taken by plants, per Sch. A-21, Exh. 26, Mcf at 16.4 p.s.i.a.				115,617,651	50,640,762	21,177,290	43,799,599
Determination of Joint Well Mouth Costs							
Total Panhandle Field Well Mouth Costs, per Line 11, page 68 of Opinion 235	$2,753,975						
Add back credit for Gas Used in Operations, per Exh. 26, Sch. A-11	167,100						
Total gas available at Well Mouth (Mcf per Exh. 26, Sch. A-21.1)	$2,921,075	129,430,635	2.256865				
Well Mouth costs at 2.256865 cents per Mcf				$2,609,335	$1,142,891	$ 477,943	$ 988,498
Gasoline Royalties, per Sch. A-21.1, Exh. 26				133,600	26,790	13,710	93,100
Total Joint Well Mouth Costs				2,742,935	1,169,684	491,653	1,081,598
Determination of Joint Gathering Costs							
Total Panhandle Field Gathering Costs, per Line 11, page 68 of Opinion 235	$1,244,758						
Texas Gathering Tax, per Sch. A-14, Exh. 26	(573,332)						
Net Unit Cost (Mcf per Sch. A-21.1, Exh. 26)	671,426	123,695,853	.542804				
Sales to Amarillo Oil Co. from gathering system (Mcf per Exh. 26, Sch. A-21.1)	(37,545)	(6,916,922)	.542804				
Net	633,811	116,778,931					
Texas Gathering Tax, per Sch. A-14, Exh. 26	573,332						
Total Gas Available from Gathering System	$1,207,213	116,778,931	1.033759				
Total Joint Gathering Costs at 1.033759 cents per Mcf				1,195,207	523,503	218,922	452,782
Total Joint Well Mouth and Gathering Costs				3,938,142	1,693,187	710,575	1,534,380
To eliminate fuel:							
Bivins—340,403 Mcf (per Sch. A-21, Exh. 26) at 3.343526 cents per Mcf ($1,693,187 divided by 50,640,762)				(11,381)	(11,381)		
Fourway—142,513 Mcf) per Sch. A-21, Exh. 26) at 3.355363 cents per Mcf ($710,575 divided by 21,177,290)				(4,782)		(4,782)	
Joint Well Mouth and Gathering Costs Allocated				$3,921,979	$1,681,806	$ 705,793	$1,543,380

[fol. 203-204]

TABLE II

Determination of Joint Gas and Gasoline Costs, Direct Gasoline Costs, and Direct Dry Gas Costs for Bivins and Fourway Year 1952

Bivins		Percent Per Exh. 34, Sch. 1 and 3	Amount
Operation and Maintenance Expenses			
Total, per Schedule A-10, Exh. 26	$211,592		
Add: 4% Labor Increase on $82,341 of Labor shown on Schedule A-11, Exh. 26	3,294		
	214,886		
Gasoline Royalties, Sch. A-11, Exh. 26	(26,790)		
Gas Shrinkage, Sch. A-11, Exh. 26	(20,300)		
Other Gas Revenues, Sch. A-9, Exh. 26	(2,200)		
Net Operation and Maintenance Expense	$165,596		
Allocated to:			
Joint Gas and Gasoline		65.94%	$109,194
Direct Gasoline Costs		26.21	43,403
Direct Dry Gas		7.85	12,999
All Other Costs			
Depreciation, per Schedule A-9, Exh. 26	$ 36,556		
Taxes—Federal Income, Per Page 68 of Opinion 235	2,017		
—State Income, Per Page 68 of Opinion No. 235	61		
—Other, Per Schedule A-9, Exh. 26	14,313		
Return at 5¾%, Per Page 68 of Opinion No. 235	35,647		
General Expenses Allocated to Bivins:			
Per Schedule A-10, Exh. 26	46,310		
Add: 3.857% (Sch. A-22, Exh. 26) of Labor Increase in General Expenses of $24,131 (4.16% of $504,611, Accts. 790 & 791, Plus 4% of $78,470, Other Accounts Per Sch. A-11, Exh. 26)	931		
Total All Other Costs	$135,835		
Allocated to:			
Joint Gas and Gasoline		78.51%	$106,644
Direct Gasoline Costs		16.37	22,236
Direct Dry Gas		5.12	6,955
Summary			
Joint Gas and Gasoline	$215,838		
Direct Gasoline Costs	65,639		
Direct Dry Gas	19,954		
Total	$301,431		

Fourway		Percent Per Exh. 34, Sch. 2 and 4	Amount
Operation and Maintenance Expenses			
Total, per Sch. A-10, Exh. 26	$114,310		
Add: 4% Labor Increase on $52,643 of Labor shown on Sch. A-11, Exh. 26	2,106		
	116,416		
Gasoline Royalties, Sch. A-11, Exh. 26	(13,710)		
Gas Shrinkage, Sch. A-11, Exh. 26	(6,803)		
Other Gas Revenues, per Sch. A-9, Exh. 26	(1,250)		
Net Operation and Maintenance Expense	$ 94,653		
Allocated to:			
Joint Gas and Gasoline		48.80%	$ 46,191
Direct Gasoline Costs		35.58	33,678
Direct Dry Gas		15.62	14,784
All Other Costs			
Depreciation, per Schedule A-9, Exh. 26	$ 50,290		
Taxes—Fed. Income, Per Page 68 of Opinion No. 235	3,961		
—State Income, Per Page 68 of Opinion No. 235	119		
—Other, Per Schedule A-9, Exh. 26	17,785		
Return at 5¾%, Per Page 68 of Opinion No. 235	70,008		
General Expenses Allocated to Fourway:			
Per Schedule A-10, Exh. 26	29,609		
Add: 2.466% (Sch. A-22, Exh. 26) of Labor Increase in General Expenses of $24,131 (See Bivins)	595		
Total All Other Costs	$172,367		
Allocated to:			
Joint Gas and Gasoline		58.3%	$100,491
Direct Gasoline Costs		31.9	54,985
Direct Dry Gas		9.8	16,891
Summary			
Joint Gas and Gasoline	$146,682		
Direct Gasoline Costs	88,663		
Direct Dry Gas	31,675		
Total	$267,020		

[fols. 205-206] BEFORE THE FEDERAL POWER COMMISSION

Colorado Interstate Gas Company

SUPPLEMENT TO PROSPECTUS DATED APRIL 2, 1952

Upon the public offering of the 966,000 shares of Common Stock to which the Prospectus relates, the several Underwriters sold an aggregate of 988,905 shares of Common Stock, at the public offering price of $26.75 per share, the additional 22,905 shares having been sold on over-allotments made in connection with such public offering. The several Underwriters intend to cover their short position of 22,905 shares, resulting from such over-allotments, (a) by purchasing from Sinclair Oil Corporation, at $27.3125 per share, flat, when, as and if received by Sinclair Oil Corporation and subject to certain other conditions, the 13,688 shares of Common Stock to be received by Sinclair Oil Corporation upon the dissolution of The Mission Oil Company described in the Prospectus under the heading "History and Business," subheading "Merger of Constituent Companies," and (b) by purchasing the remaining shares in the open market.

* * * * * * *

[fols. 207-210] BEFORE THE FEDERAL POWER COMMISSION

TRANSCRIPT OF TESTIMONY

Q. Now, will you look at Exhibit No. 1, Mr. Wiskup, and the first schedule that you are sponsoring is Schedule No. 3; isn't that so?

A. Yes, sir.

* * * * * * *

[fol. 211] COLLOQUY BETWEEN EXAMINER AND COUNSEL

Mr. Goldberg: I say if it is a matter of law, why not let us close the record and brief this question of law. Why go through the whole process of cross-examination, and every-

against us, so that if the proceeding reaches a point where we put in our own case in chief, we know what contentions we have to meet, and what we have to controvert.

I submit under the exhibits here we do not have such notice. We do not know whether we are dealing with 1951 on the basis that the staff purports to deal with it, or 1952, or 1953. It does not appear that they have attempted to accumulate in any particular actual period of time such future adjustments as might be necessary to be made in order to intelligently fix future rates, so I submit, *sir*, we are entitled to notice under any type of orthodox procedure, so that we know what contentions we have to meet.

Now, that is the first inquiry I have to make, and I think we are entitled to that answer. I would appreciate it very much if we could have that issue resolved, and then I have another statement to make.

Presiding Examiner: By what method do you propose to get it. By cross-examination?

Mr. White: That is something I don't know, but I think under the rules of any orthodox procedure, as I pointed out, it is not necessary to resort to the method of cross-examination to get all of the fundamental contentions that are made against us. It seems to me that the type of notice which a person is entitled to is notice which appears from the pleadings. Pleading may be amended by evidence, but the evidence, I submit, which would make a case for them, upon which to stand, it is their duty to elicit upon their direct examination. They have not done that. We don't know what to cross-examine on. We might have [fol. 216] to cross-examine on all three years, we might have to prepare on all three years. We don't know exactly what is being contended against us, and I submit, sir, in the absence of pleading, that should be made evident upon the record before we have any obligation to proceed further in the matter, whether by cross-examination, or otherwise.

Presiding Examiner: Mr. Goldberg?

Mr. Goldberg: I think that Mr. White misconstrues the full import of a rate proceeding, Mr. Examiner.

I think it should be clearly understood that it is the Commission that fixes rates, based on all the evidence and all the record before it and I wish that fixing rates were an exact science, so that we could give Mr. White the exact pleading that he contends for. Unfortunately, fixing rates is not an exact science. It involves questions of judgment. Counsel here have taken issue with the evidence that we have presented of actual experience, and wanted some evidence as to the future facilities. We have done our best to supply evidence on that score, and I think that that is all they are entitled to get.

* * * * * * *

Mr. Goldberg: The thing can be answered two ways, and that is why I preferred to leave it to the body that decides to determine which approach they would take.

Presiding Examiner: Does that mean that the staff isn't going to recommend anything to the Commission?

Mr. Goldberg: No, sir, we are not going to recommend anything.

Presiding Examiner: Well, right now is the time to let us know what your position is.

Mr. Goldberg: Our position as to the use of this material is as follows, Mr. Examiner. You can do it either the way your Honor suggested, use this new material to adjust the figures for the actual, or you can do the reverse, you can use this new material and adjust that by the actual, and [fol. 217] frankly we have not made up our minds which is the approach. Obviously it is either one of the two, and we are not in a position to say which is the method that should be followed.

Mr. McGee: I am all confused. I think we have reached a point in this proceeding where we have to stop, look and listen.

I think that some day in the future, I am sure, the case will be presented that is understandable, that can be an-

swered, and one upon which we can present a case of our own. I will be frank with the Examiner and state that up to this period we have been unable to determine what we should do. We don't know how we can prepare for cross-examination, we don't know what sort of a case to prepare ourselves.

I have never experienced anything like this before, such secrecy or hesitancy. If the staff hasn't made up its mind what to do, it is their case, it is the Commission's investigation, we didn't start this. We are on the defense. Now, what are we to defend against?

Presiding Examiner: I don't think secrecy is any longer involved. Mr. Goldberg has stated two possible ways, and that the staff hasn't as yet determined whether to use either or both. Isn't that correct, Mr. Goldberg?

Mr. Goldberg: That is quite right.

Presiding Examiner: There is no secrecy. There may be uncertainty, but no secrecy.

Mr. McGee: I said hesitancy, too.

Is Mr. Goldberg standing on the test year of the original case? I haven't got the direct answer to that yet.

Mr. Goldberg: Well, our answer is we are not standing on anything, except all the evidence that has gone in. That is simple enough. It is an investigation, as you said, Mr. McGee, and we present all this testimony for the Commission's consideration, including past experience and the company's estimates for the future.

. . . . . .

[Tod. 218] Presiding Examiner: It seems to me Mr. Goldberg answered the question the Examiner had, and that is the possible interrelation of this material to his other case. The fact he stated in the alternative it may not be as easy to work with, and wouldn't be if I had to work with it right now. Suppose everybody would quit right now and say to the Examiner, "It is your baby to decide and write an initial decision," it wouldn't be easy to work with, but he has told me what I can start working on. I think he

has answered the essentials that relate to the process of carrying the burden of proof. That is what it comes down to, because actually everything you are saying—I didn't take up the question of whether they sustained the burden of proof. I did say it seems to me the Examiner would have to have some indication, or should have—I wouldn't say have to, but should have some indication as to the possible relation of this material to the material in the earlier portion of the direct case, and he has answered that. He has answered, as I understand it, in two ways. You can use it either one way, or the other, which he outlined.

So far as the question the Examiner asked for his own assistance, I think that that is answered, and I think that if you challenge the matter of burden of proof, whether you sustain the burden of proof, that was the basic problem at one time, and always until counsel rests, and then I suppose it becomes a question of whether or not he has, but that is an ultimate question.

* * * * * * *

Presiding Examiner: Well, that only bears on whether or not you need time to study it. You have got all the notice that the facts of the evidence now give you, plus his statement that this new material can be used either to adjust the calculations in the base year, or vice versa, so it really boils down to how much time you think you will require, [fol. 219] first, in connection with cross-examination.

Mr. White: Before we get to that point, Mr. Examiner, I wish to notify the Examiner and all present that we are going to file a written motion in the nature, again, of a demurrer to the evidence, contending that the staff has not met the burden of proof, and as a matter of law has not shown such facts upon which a rate order may be based.

Mr. Goldberg: May I point this out on the record, Mr. Examiner:

Your Honor is aware that this is not a situation where the company has filed for a rate increase, and it has been suspended, or they are collecting increased revenues under bond. This is a Section 5 proceeding, which looks toward

a reduction in rates, and for every day's delay there is a certain amount of excess revenue that is being collected from the ratepayers.

Mr. White: Assuming that is correct.

Mr. Goldberg: There is nothing I can say about stopping counsel from filing motions, but I don't think that the progress of this hearing should be impeded by any motion that counsel may offer to file.

* * * * * * *

Presiding Examiner: We will recess, then, until November 27, subject to further order of the Commission if they should wish to change it.

We will recess, of course, to 1800 Pennsylvania Avenue, N. W. in the main hearing room, on November 27.

Whereupon, at 12:33 o'clock p. m., a recess was taken until 10:00 o'clock a. m., Tuesday, November 27, 1951.

* * * * * * *

[fol. 220] William F. Spurrier was recalled as a witness, and having been previously duly sworn, was examined, and testified further as follows:

Cross-examination.

By Mr. White:

* * * * * * *

Q. Now, what method of costing this natural gasoline plant operation did you use in Exhibit 1, Mr. Spurrier?

A. Primarily the relative market value.

Q. And would you tell me why you selected that method?

A. In selecting a method for the allocation of these joint products, we set up a standard of, first, the results must be reasonable, that whenever the result is obtained on that basis it must make common sense.

The second basis, it must be a generally accepted method for allocation.

A third was that the allocation, or the results of the allocation be realistic in the light of the conditions and the economic conditions that presently exist.

* * * * * * *

Q. Now, do you feel that the relative market method which you used meets all of these results? I think you testified that you did, is that correct?

A. There is no method, Mr. White, that you could use that would give a refined answer to this. It was the method that in my opinion reflected the conditions as they existed, the nearest.

Q. All right, did you feel that it met more nearly than any of the others the test of reasonable results?

A. Yes.

Q. And did you feel that it was a generally accepted method?

A. Yes.

Q. And did you feel that it was realistic in the light of economic conditions?

A. Yes, I did.

* * * * * * *

[fol. 221] Q. Well, now, Mr. Spurrier, by using the averaging process you would never know exactly what costs are attributable to your product on the basis of the selling price at that particular time, would you?

A. Well, it would be impossible, Mr. White, to devise any method that is going to be letter perfect, and it would give you a reasonable answer.

Q. All right, let's find out.

Presiding Examiner: Mr. Spurrier, I don't think that answer was responsive to the question. It may be a good answer, but it wasn't responsive to that question.

The Witness: Well, Mr. White, were you satisfied with it?

Mr. White: Let me decide. May I have the question read back, please?

(Question read.)

By Mr. White:

Q. The answer is no, is it not, Mr. Spurrier?

A. I would say the answer was it would give you a reasonable result.

Q. You stated you examined Exhibit 45 in Docket G—Mr. Houlihan's study in the merger case, which is Item B by reference here?

A. That is right.

Q. Do you recognize, or do you not, that Mr. Houlihan's study was based on an actual analysis of the operations of the gasoline plant, the Bivins gasoline plant of Canadian River Gas Company, with a view to costing it on his volumetric basis?

A. I don't know what Mr. Houlihan actually did. I know generally speaking he used the volumetric basis——

Q. Is your answer that you don't recognize that he did?

A. I don't know what he did.

Q. You say you read his testimony in that case.

A. That is right.

Q. Did he state that he did?

A. He stated—well, I can't recall exactly what he stated. [fol. 222] If I remember correctly, I believe he said he spent some time in Texas, six days, one of which he was marooned, or something like that, but whether that would be sufficient for him to make the study you outlined, I don't know.

Q. Well, can you describe for me, Mr. Spurrier, roughly the method used by Mr. Houlihan?

Mr. Goldberg: I object, Mr. Examiner.

Presiding Examiner: Why?

Mr. Goldberg: Well, Mr. Houlihan is the man to tell us what his method is. I don't believe this witness should be called upon to tell us what Mr. Houlihan did.

Mr. White: I think the witness stated he considered among other things the examination of that material to which I am now referring for his presentation in this case.

Mr. Goldberg: In that case the best thing would be to incorporate in Houlihan's testimony. Then everybody could read it.

But to get this witness to try to tell us what Mr. Houlihan said in another case is far beyond the scope of this or any other witness.

Presiding Examiner: Well, now, let us just get the whole thing in front of us here. This witness is supporting a certain method. He has turned down the other method, he stated so, he didn't like it.

Now, is there any reason why he shouldn't tell us all about it, why he didn't like it, why he thinks one method? I have just sat here for two days and heard experts cross-examined by the staff. They didn't duck any questions. They were willing to meet anybody's methods and study them comparatively and give this Commission the benefit of it. Is there any reason why he shouldn't?

Mr. Goldberg: Quite right. All Mr. White has to ask is why he didn't take the volumetric method. But to get this witness to try to interpret what Mr. Houlihan said is not the way to do it. All he has to do is ask him a straight-[fol. 223] forward direct question, why did you adopt the volumetric method, period.

Mr. White: That has been done, Mr. Examiner, and the witness has set up certain tests which he feels a method must meet, and I think it is perfectly appropriate for me to see if this man comprehends the method, which he says he has studied and considered in preparation of this study of his.

Presiding Examiner: There might be various ways of doing it, but there is no reason why this witness shouldn't tell us what he knows about Mr. Houlihan's method, and why he didn't like it, and all about it. The Commission needs to have the comparative side unless you want to load the dice, and I am sure that isn't in the cards. Do you know what his method was?

The Witness: I read what his method was.

Presiding Examiner: Well, do you know now?

The Witness: I know he used a volumetric method, but I don't know just what mechanics he went about. I know he uses a volumetric method in which he took the various percentages of the methane, butane, propane, and then took the percentage afterward, and I discarded that—that is, I considered it, and I thought it was not representative of

the facts, any more than it is representative of the fact when you buy a ton of ore, and you split the value of the ton of ore between gold and some other metal in there on the basis of weight.

It has no relationship to the basis of weight, and I say the product, the dry gas and the gasoline, the allocation of the cost is nearer the true picture by using the relative market value than it is the volumetric basis.

By Mr. White:

Q. We are just dealing with Mr. Houlihan's study at the moment.

A. I understand Mr. Houlihan's is the volumetric method. I don't know all the details he went through to arrive at that.

[fol. 224] Q. Do I understand you, Mr. Spurrier, recognizing it was the volumetric method, discarded it for that reason?

A. Not for the reason that it was a volumetric method, period, I discarded it. I looked at the volumetric method, not only Mr. Houlihan's but the volumetric method that would apply to a number of things. For instance, in the packing industry——

Q. Now, tell me—I don't mean to interrupt if you are not through with your answer.

A. Go ahead.

Q. Tell me just what analysis you made of Mr. Houlihan's method?

Presiding Examiner: Or of the volumetric method, no matter whose it is. He just happened to use it. It is a standard method, he just happened to use it. The question is whether it is standard in this type of thing or not.

The Witness: My analysis of the volumetric method disclosed there was a relatively small amount on the volumetric method that would be associated against the gasoline, which, while it is a recognized method in some respect, the fact that a small amount of joint costs would be allocated against the gasoline, a product that commands a fairly good price, I felt didn't reflect the facts.

By Mr. White:

Q. Then do I take it that you looked at the result of the volumetric method?

A. No, I looked to see what amount of volume was involved, just like in a ton of ore. When you weigh the gold it is very small amount. You would look at that and say, "I am not going to accept that, because that doesn't square with the facts, although it is a recognized method." When I looked at the volumetric method, I said there is a small amount of volume involved in this for the value of the product, therefore I don't quite like that method. It allocates such a small amount to the 35 million gallons of gasoline that come up there that I said there must be something wrong with the method.

Q. Did you feel that method did not square with the facts?

A. The volumetric method?

[fol. 225] Q. Yes, either the volumetric method generally, or Mr. Houlihan's application of it.

A. I felt that the volumetric method as contrasted with the Btu method, and also the relative market value, that the best results would be obtained by using the relative market value.

* * * * * * *

Q. Now, Mr. Spurrier, after your review of the material that you made on cost accounting, for joint products, could you tell me whether there is any method that would result in higher cost being attributed to natural gasoline than the relative market value method?

A. Oh, I suppose there are other methods——

Q. Do you know of any?

A. Well, I think that there would be variations of the market value, that is it could be gross market value instead of deducting the amount that was cost to make marketable, if you used a basis like that—and it is not without reason—might result in a greater amount being assessed against the gasoline.

Q. Now, wait. If you used—if you deducted from the natural gasoline the cost to make it marketable——

A. That is if you did not deduct it.

Q. Oh, if you did not deduct it.

A. In other words, that would be the ratio——

Q. Did you deduct it here?

A. Yes; in determining the ratio, we deducted from the revenue derived from the sale of the gasoline the cost to make it marketable, in determining the ratio between dry gas, and the gasoline. Now, answering your question more specifically, I suppose if we hadn't deducted that, and had used the gross sales price and related that, and used that figure in determining the percentage, it would have arrived at a higher figure, but the usually accepted method in the allocation of joint products is if your joint products reach a certain point, that cost is allocated between the product. The portion to make it more marketable applies to that specific product, not to the joint product. Although sometimes they do use the gross sales value.

[fol. 226] Q. Aside from that, would there be any method that would result in a greater cost being assessed against the natural gasoline operation that you know of?

A. Oh, I suppose you could——

Q. Now, I ask you do you know, Mr. Spurrier?

A. Do I know specifically of another method?

Q. Yes.

A. Well, I didn't approach it from that angle.

Mr. White: Mr. Examiner, I think my question is susceptible to a yes or no answer, and I ask that the witness be instructed to answer accordingly.

The Witness: I will say yes, but I don't know that there is no other method.

* * * * * * *

Mr. Goldberg: We will supply that information, Mr. Examiner. You can get down off of there, Mr. Spurrier.

Mr. White: Wait, I have some questions on recross.

Presiding Examiner: You did not state that you had completed your examination. The Examiner will excuse the witness when the time comes and he has determined that the witness is no longer required. There are certain amenities that counsel might follow.

Mr. Goldberg: Mr. Examiner, there is $10,000 a day for every day's delay. We are anxious to conclude this hearing, too, remember that, sir.

Presiding Examiner: Is there any recross?

Mr. White: Yes, there is, sir. I have a few questions.

Presiding Examiner: Your may proceed, I hope without further interruption.

* * * * * * *

Further cross-examination.

By Mr. McGee:

* * * * * * *

[fol. 227] Q. In arriving at the reasonableness of your theory, did you test any other theory to ascertain which of the theories would produce the largest excess revenue figure?

A. I considered the volumetric basis, and the Btu basis to determine what percentage of the joint products you might allocate to, as I said yesterday, 35 million gallons of gasoline that was extracted from the Bivins and the Fritch plant, and any basis that allocated an unrealistic amount of those joint costs I would say did not meet the test, number one, nor it did not meet the test number three.

Presiding Examiner: Of course you are begging the question when you say it isn't realistic. I am not at all sure when you stop and sit down and analyze this and say you are going to test this by reasonableness as to whether or not you haven't begged the whole question to start with.

The Witness: Let me say this: If you sold a product in the market today for several million dollars, and it was a joint product and you allocated against that product an infinitesimal amount of the joint costs, the answer would have to be unrealistic.

Presiding Examiner: Maybe. That may be your——

Mr. Goldberg: That is your opinion, is it not?

The Witness: That is my opinion. They got 35 million gallons——

Presiding Examiner: Aren't you testing your method not by intrinsic accounting principles, but by what result you

get out of it, whether you like it or whether you don't like it?

The Witness: I say there are no refined accounting principles that you can apply to this problem as any writer will say. After he illustrates a method, he is the first man to say there is some criticism that can be made of that. Now, there is no magic formula you are going to apply——

Presiding Examiner: Nobody is talking about magic.

The Witness: You used the word "principles."

[fol. 228] Presiding Examiner: In other words, all I am trying to confront you with, so that you can improve your own testimony, is this: In your answer a minute ago, in answering whether or not it was unrealistic, you used the fact that you already concluded it was unrealistic. Now, I merely pointed out that that raises a question as to whether or not, when you set up one of your three standards as to whether or not it is reasonable, and test as to whether to use this method or that method, by that kind of a standard, as to whether or not you are not begging the question to start with. I am asking you to consider that.

The Witness: I don't think I am begging the question and more than you do when you say we will buy a ton of ore and allocate the cost of the ton of ore between gold and the other metal on the basis of weight, which is the accepted method under some procedures, but certainly wouldn't be in that case. Now, I say any result that you take, it is an accepted procedure to use it on that basis, but the result would be so far out of line that you would dismiss it on the first reason, that was unrealistic.

Presiding Examiner: I didn't mean to interrupt your testimony. I thought you might have an opportunity to correct your own statement there.

The Witness: I don't think that I have any statement to correct. This is the best basis, after considering the volumetric basis, the Btu basis, that I was able to determine, and Mr. McGee, don't think for one minute that we didn't realize that we would be sitting in this chair hours over that situation, and the path looked pretty smooth for us to say, "Let's use some other basis," but you have got a principle here that should be set forth, and that is that the volu-

metric basis, and the Btu basis violate the first principle, that it doesn't give an answer that makes common sense.

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Q. Is it not a fact that aside from the contract, in order [fol. 229] for the gas to be made marketable that that process has to be done? Now, that is a simple question, isn't that a fact?

A. I would say that whether you use marketable——

Q. Transportable, use that.

A. Transportable. Now, that is an engineering question, and my answer to that is this. As I understand it, they tried from the Hugoton line to transport the gas without that small plant that they have there, and they finally had to put it in. The amount of gasoline that they extract per Mcf is about a quarter of a gallon per thousand Mcf, as I recall it.

Q. You mean per thousand cubic feet, or thousand Mcf, which is it?

A. Per Mcf. Now, when you get to Bivins, they extract about a third of a gallon. At Fritch, nearer a half. Now, if they were unable to transport the gas in Hugoton by only taking a quarter, it was an engineering necessity in the line of efficiency to take it out, then I could assume that they couldn't transport the gas without operating difficulties from Bivins, but I don't know whether from the standpoint of an engineering situation whether they could or whether they couldn't.

Q. That is an awful long answer to a simple question, but I gather from what you say that from the facts at hand, it would at least appear necessary to process the gas in order to make it transportable.

A. From the facts when you consider the gasoline in Bivins and the other, I would say yes.

Q. All right, we have got that.

Presiding Examiner: Let's evaluate that as we go along. This witness is an accounting witness, not an engineer. He doesn't have any opinion, the truth of the matter is, because any opinion he would have would be as an amateur. He is an amateur in the field of engineering. He is an ex-

pert in the field of accounting. Therefore, all he is saying in regard to your questions now as to whether it is necessary or not, is that he has done his work on the engineering assumption handed to him, plus a legal assumption handed to him that the extraction is required, is that right?

The Witness: That is right.

Mr. McGee: And I accept that.

[fol. 230] Presiding Examiner: All right.

* * * * * * *

Presiding Examiner: * * *

Suppose they make a profit? Is that a credit to the ratepayer? Is your accounting that it would be a credit to the ratepayer?

The Witness: Of course that is something the Commission would have to decide. As it was handled before, it was credited to any gasoline that was extracted less the cost of extracting it. If it was a profit, it was taken with revenue in determining revenues subject to the Commission's jurisdiction. What they are doing now——

Presiding Examiner: You are using an accounting method. I am trying to find out whether your method, in your own thinking, is one cut and fit to reach particular results, or whether or not it is applicable universally in this set of facts. I have changed one factor only, that is all, and that factor is that instead of making a $295,000 loss, Colorado Interstate, under all the same facts it made the loss on, makes a profit of $295,000.

Now, at the present time the results of your accounting, and therefore your recommendation to this Commission as an expert hired by the Commission to advise it, is that Colorado pocket that loss, and that the stockholders pocket it and have no chance to recoup it, isn't that right?

The Witness: That is my understanding of what the Commission said——

Presiding Examiner: All right, now, let's take the converse. If they make a $295,000 profit instead of a loss, is it the application of your mode of accounting, now, does that mean they can put the $295,000 profit in their pocket and keep it?

The Witness: Well, my handling of it here would be ex- [fol. 231] actly the same. The revenue would go in, and the loss would go in. The revenue—whereas before the merger——

Presiding Examiner: Is that jurisdictional revenue?

The Witness: I would put it in as jurisdictional revenue——

Presiding Examiner: You would put the loss is as jurisdictional revenue?

The Witness: It took the loss in and did not consider it a cost of service, because as I read the order, that is what the Commission said. When the 50 percent no longer processes the whole, that can't be considered as an item in the cost of service.

Presiding Examiner: All I am trying to ask you is what would your advice be to the Commission if the reverse facts were true, that is all. Would it be jurisdictional revenue, or not?

The Witness: Considering the entire situation with respect to Colorado Interstate, and Canadian River, if that was a $295,000 profit, it would be in the revenue along with the gas revenue.

Presiding Examiner: In other words, if it is a loss, they pocket it, but if it is a profit, they have got to account to the ratepayers for it?

The Witness: That is exactly right, Your Honor, because at one time before the merger they had 100 per cent of the profit. Southwestern got none of it. It was on this basis that they said, "We are going to merge these properties," and the Commission says, "Give up 50 per cent of this revenue, give it up, but in giving it up if it results in a loss to you, you can't add it back to the consumer."

By Mr. McGee:

Q. And didn't the Commission say that because the company offered that as a stipulation?

Presiding Examiner: I want to see if this accounting carries through straight line, or, as I say, it is good if you get certain results, and not good if you don't. That

is all I want to know. I think that is of some vital importance in evaluating the method in comparison with other [fol. 232] methods that might be available.

The Witness: Have I answered when I say the $295,000 would be taken in as revenue along with the other gas revenue, if it was a profit, the same as it was when it was a profit as it existed, and as it exists today without the merger being consummated.

Presiding Examiner: And thereby they would have that much more excess revenue.

The Witness: Yes, sir. It is a jurisdictional revenue that the Commission has decided before, as I recall it, and has taken it in. Now, I would put the item in exactly the way it was. I wouldn't vary my method of allocating cost on a relative market value merely because it has been suggested that it went to a profit instead of a loss. That would have no bearing so long as the other standards were there, the three other standards.

Presiding Examiner: Now, don't in any of these situations, don't imagine I am trying to reach any results here. I am trying to anticipate the position I might be in if you didn't answer some of these things, and I had to guess the answers, because this is a very good illustration. I would never have guessed your answer.

Mr. Goldberg: May I ask a clarifying question, Mr. Examiner?

Mr. McGee: May I proceed?

Mr. Goldberg: Oh, go ahead, I don't care.

Mr. McGee: Ask your question.

Mr. Goldberg: In order to arrive at $295,000 profit on these gasoline operations as the Examiner suggests there might be a profit, you would in the beginning have to allocate the joint costs according to the relative market value precisely in the same manner as you did it here.

[fol. 233] The Witness: Exactly. The fact that it went to a profit or a loss would not change my method of allocation.

Mr. Goldberg: All right, thank you, Mr. McGee.

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Presiding Examiner: Let's answer what I have got now. You are trying still to answer his question. Just answer my question.

The Witness: Read that back, will you?

Presiding Examiner: It is a simple thing. They process a certain amount in order to make the product salable.

The Witness: Yes, but there is where we have difficulty.

Presiding Examiner: And they don't sell it.

The Witness: If they just have to take it out to make it transportable, they don't have to incur all the extraction costs that are in here.

Presiding Examiner: I am not talking about the book figures, I am talking about one simple example. This is certainly not a case of a confusing question.

The Witness: As I understand it there, you are coming out with a natural gasoline of 26-70. That is what you are saying——

Presiding Examiner: I don't give a damn what the gasoline content is. I don't care what kind of gasoline it is, because in my assumption they throw it in the ditch. They don't sell it.

The Witness: My answer to you is that they would never incur the cost to make marketable. They would—all of those costs which are shown on Schedule 6——

Presiding Examiner: You are not answering my question at all, you are just arguing the case now. I am trying to get this thing so we can get somewhere instead of just a lot of confused answers.

[fol. 234] It is a very simple proposition. It boils down just as simple as this. You have got to take the hides off of beef to sell the beef, if you are going to cut it up and store it and sell it through marketable channels.

The Witness: That is right.

Presiding Examiner: And there is no market for hides.

The Witness: Yes, your Honor, I am with you there.

Presiding Examiner: Now, the cost of taking a hide off is a part of the cost of producing the beef.

The Witness: Yes, sir.

Presiding Examiner: That is all I am talking about here, that is the first illustration.

The Witness: All I wanted to be sure was that you weren't taking into consideration the cost to tan that hide and found no market.

Presiding Examiner: I am going to throw it in a ditch.

The Witness: But you used the term "natural gasoline." At that point, there would be no market value for the gasoline, because you didn't sell any, and all of your costs would be associated against the gas.

Presiding Examiner: All right, let's take the next step.

Mr. McGee: May I have that answer read?

(Answer read.)

Presiding Examiner: Mr. Spurrier, we want to take this step by step to see how your method operates, what your conception is.

The Witness: I appreciate that, but after it is in the record, it speaks for just exactly what it says, and if in the confusion I answered a question which involved the processing of the gasoline within the gasoline plant, which wasn't necessary, to dump it, then I am stuck with that part [fol. 235] of it, and all I want to say is your best example was the hides, if you strip the hide off, throw it away, that is it. But if you tan it and then throw it away, that is a horse of a different color.

Presiding Examiner: Actually, the example I gave you is exactly the converse of what is happening in Colorado right now, at Rangely Field. The State Commission has just put out some conservation orders to say that they can't produce oil with more than a certain amount of gas in it, and flare that gas.

Certainly the cost of processing the oil out of the well so as to make the heavy oil transportable is a cost of producing the heavy oil, isn't it, and they flare the gas?

Now, the converse is the case of where the gas coming from the field is so wet, it has such a degree of heavy hydrocarbons, that some of it has got to be taken out, and if you don't do anything with those, then there is certainly no problem here but that that is a cost of service of the residue gas.

The Witness: Just like taking sulphur out.

Presiding Examiner: That is right, exactly. I started to use the sulphur illustration, but I figured sulphur was so blamed valuable you couldn't hardly assume you couldn't sell it since there is a world shortage on it right now.

Now, the next step is—and this begins to give you an opportunity to explain the difference, which was bound up in Mr. McGee's question.

In fact, they process more than is essential to transport the residue natural gas to markets, and they sell it. Now, how much of the total cost of the extraction of both that which is necessary and that which is unnecessary, is properly chargeable to cost of service.

The Witness: What I would do is take the total amount of gasoline that was extracted, regardless of whether it was necessary, plus the amount that you took out, the total revenue that was derived from that, from that I would deduct the cost to make marketable, I would determine a relative market value on that basis. It doesn't make any [fol. 236] difference whether the gasoline that you sold this month you had to take out, under your example to make it marketable, or whether you took it out because the gas was high Btu, and you could put it in the line at a lower Btu. It wouldn't make any difference with the relative market value theory, and if I may say one thing more. If you throw it in the river, as you say it, and you are using——

Presiding Examiner: In the second illustration, I didn't throw anything away. I sold it all.

The Witness: In the first illustration, where you said you dumped it in the river, if you take the Btu basis, or the volumetric basis, regardless of what you did with it, you had to allocate a cost against it, but the relative market value, if you dump it in the river, assesses all of the cost against the dry gas. The other two methods fall down in this phase, but it is so difficult——

Presiding Examiner: Well, now, I think we have got fairly clearly two steps of this. In the first illustration they didn't sell any of it, and they only processed that which was necessary, so naturally the gas went to cost of service.

The Witness: Under the relative market value, it went to the cost of service.

Presiding Examiner: Now, in the second illustration, they processed more than was necessary, and sold it all. In that case you say you would apply your method, and you would not count any part of that as cost of service.

Mr. McGee: Except dehydration.

Presiding Examiner: I am not talking about dehydration now. Let's don't get into that. That is really just a necessary element. The only reason it is treated the way it is here as far as I can figure out is that it is admitted by everybody that it is necessary to do some dehydration, and you don't sell the water you get out, so that is the first illustration.

[fol. 237] Mr. McGee: This dehydration we have been talking about is not the same type of dehydration that we think of in connection with the operation of a big dehydration plant.

Presiding Examiner: I don't want to get into complexing details. I want the straight line series of questions to illustrate his use of this method.

The third illustration modifies the second only to this extent, and it is very simple, it seems to me. They again process a little more, or some more than is necessary, and they sell not all of it—they haven't got a market for all of it. They sell only that part—it just happens that they are able to sell that which it was necessary to extract, and they have to throw the rest away. Now, how does your method apply?

The Witness: Exactly the same way. I say the market value is determined from what you actually sold, deducting the cost to make it marketable, as related to the total value of the dry gas, and the total of both of them determines the relative market value, and I wouldn't change the basis because I think it reflects the facts as they exist.

Presiding Examiner: Now, in the third illustration it wouldn't make any difference whether you used a 20 million total, with 10 necessary, and 10 unnecessary, to be extracted, and sold 10 and didn't sell 10. In other words, you can put those figures in there, and you have got your answer now to the question he asked you, haven't you?

The Witness: That is right. I have my total revenue regardless of the number of gallons sold. I have got my cost to make marketable which gives me a figure which is the actual revenue from the gasoline sales—no, that is the net, that in relation to the total revenue is the percentage that applies to the joint products.

Presiding Examiner: I think that brings us up now to get your answer, in a form that i can begin to understand what he says.

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[fol. 238] FRANK S. FRENCH was recalled as a witness, and having been previously duly sworn, was examined and testified further as follows:

Cross-examination.

By Mr. White:

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Q. Now, I think you already have stated that you are the same Mr. French who testified in Docket G-462, which was the subject of that review, aren't you?

A. Yes, sir.

Q. And you also are familiar, are you not, with the opinion of the Commission which we referred to this morning involving the Mississippi River Fuel Corporation in Docket G-462; is that correct, sir?

A. With certain modifications.

Q. You mean you aren't familiar with it—I am only asking if you are familiar with it.

A. Oh, yes.

Q. Mr. French, would you say that your cost classification in this case is similar to and consistent with your testimony and evidence in Docket G-462 in the Mississippi River Fuel case?

Mr. Goldberg: I object, Mr. Examiner.

Mr. White: If your Honor please, I think that prior inconsistent statements is one of the orthodox ways of probing a witness on cross-examination, and I am only asking

him to say whether they are or are not. He has a recollection of the case.

Mr. Goldberg: Mr. Examiner, he asked him what prior inconsistent statements he made. I think it is up to counsel to direct his attention to prior inconsistent statements. I don't think it is up to counsel to ask this witness what prior inconsistent statements he made.

Presiding Examiner: Read the question. It wasn't phrased in quite that way.

[fol. 239] (Question read.)

Presiding Examiner: I can't see any possible basis for objection. There is nobody in the world knows any better than he does, and he might have very deliberately made it slightly inconsistent and have good reasons for it. He has lived some years and had some cumulative experience.

I think the witness certainly has the competence to answer the question, and it certainly is a relevant question.

Mr. White: I think so, too.

The Witness: The cost classification as set out here is not similar to the cost classification as ordered by the Commission in the Mississippi River Fuel, Docket G-462.

By Mr. White:

Q. Would you say that your cost classification in this case follows the principles enunciated by Judge Prettyman in the opinion to which we referred, which is reported at 163 Fed. Secd.?

A. I don't wish to interpret Judge Prettyman's decision.

Q. Would you say that your cost classification in this case is similar to and consistent with the classification of cost used by the Commission in its opinion in Docket G-462?

A. Very closely, with minor exceptions which, for the reason of consistency, I have made the change.

Q. Would you also say that your cost classification in this case is similar to and consistent with your evidence on cost allocation in the presently pending proceeding involving the Mississippi River Fuel Corporation, Docket G-1641?

A. With the exception, I believe, of a little different treatment on the spreading of customer costs, but it is very minor, and it certainly is the same in the Hope case which was recently put out by the Commission.

Q. Now, in the Hope case, was there any difference between the company and you, any fundamental difference on the question of cost allocation?

A. Apparently not, because they didn't ask me any questions. They put depreciation 50 per cent to commodity and 50 per cent to demand, and compressor station labor was 100 per cent to commodity, and maintenance to com- [fol. 240] pressor station equipment as 100 per cent to commodity.

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Q. I refer you now, Mr. French, to Table IX of your Exhibit No. 10, sheet 5 of that table, where there is shown the detail for the total administrative and general expenses which you have referred to before, will you explain what relationship there is between the amount shown for special legal services of $44,690, the amount shown of $13,460 as regulatory commission expense, or the amount shown for maintenance of communication equipment, of $75,118.61.

A. Was your question what——

Q. What relationship is there between those amounts?

A. I don't know what you mean, special legal service is one thing——

Mr. White: May I have my question read. I think maybe I fouled it up.

(Question read.)

Mr. White: I think I had better rephrase that.

By Mr. White:

Q. Will you please explain the relationship between the amount shown for special legal services of $44,690.47, the amount of $13,460.83 as regulatory commission expense, or the amount shown for maintenance of communication equipment of $75,118—the relationship of those—to labor, materials and supplies of transmission.

A. I made no individual account studies of administrative and general expenses.

Q. Now, did you not in the Mississippi River Fuel case, Mr. French, give recognition to the fact that administrative

and general expenses are not only related to labor and materials, but also to return, depreciation, taxes, and in fact to all cost of service, exclusive of administrative and general expenses?

A. I didn't state that in the Mississippi River Fuel case.

[fol. 241] Q. Was that the effect of your treatment to the Mississippi Fiver Fuel case?

A. It is not.

Q. Was that the effect of your treatment in the old Mississippi River Fuel case in Docket G-462?

A. It is not.

Q. Do you have a copy of Exhibit No. 10 in Docket G-462, Mr. French, with you?

A. No.

Q. Would you recognize it if I showed it to you?

A. Yes, sir.

Q. I ask you if this isn't that document?

A. That is correct.

Q. That was an allocation study of yours in that docket, was it not, Mr. French?

A. That is right.

Q. Now, will you turn to sheet 2 of Schedule 4 therein, Mr. French?

A. All right.

Q. And I will ask you to state whether or not you didn't classify administrative and general expenses in accordance with all cost of service, or only in accordance with transmission labor and supplies?

A. You mentioned something about depreciation, taxes, and all that. I have not used any different method in the original Mississippi case than I am proposing in Exhibit 10 of this case. There might have been some items of expenditures appearing in one case that might not have appeared in the other but I have been entirely consistent. I might correct that to one extent there. It doesn't appear in that case—and I can't give you the reason why—we don't seem to have allocated general and administrative expense to its cost classified as "other." It appears we only allocated that to demand and commodity, and dropped out the other.

Q. Was that done on the basis of total cost, or just on transmission cost?

A. Of course in the case of Mississippi, they didn't have anything but transmission. They had no production.

Q. Well, you had total costs which included return and depreciation.

A. Oh, no, just total transmission cost. Everything else was so-called below the line. The way I would classify it, [fols. 242-248] maybe not an accountant—in other words, not the direct transmission costs, and when I speak of that, I don't mean the items such as depreciation and taxes and return. The allocation of administrative and general was made prior to the determination of the cost classification of that type of item.

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[fol. 249] ALEXANDER E. WISKUP was recalled as a witness, and having been previously duly sworn was examined and testified further as follows:

Direct examination.

By Mr. Goldberg:

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Q. Mr. Wiskup, will you please turn to Schedule A-1 of Exhibit No. 26 for identification, and tell us what that is, please, sir?

Mr. White: If your Honor please, before the witness proceeds to answer, I ask from staff counsel an offer of what he intends to prove in this rebuttal case from Exhibit 26 for identification?

Mr. Goldberg: Mr. Examiner, this exhibit is an exhibit based on the cost of service study introduced by Mr. Jones for the company, which is Exhibit 21, and it shows the adjustments which the staff has made to the cost of service study introduced by the company.

[fol 250] Mr. White: May I inquire of counsel if that is all it shows, and is that all it is offered to show?

Mr. Goldberg: Well, considering the adjustments, of course, it shows that the excess revenues are larger than the excess revenues shown by Mr. Jones.

Mr. White: And with that addition, sir, is that all it is offered to show?

Mr. Goldberg: I am not going to be bound——

Mr. White: I am curious, sir. I submit to the Examiner that we are now engaged in the rebuttal case by which the staff is, I assume, to rebut the case in chief put in by the respondent, Colorado Interstate Gas Company.

I submit that on the fact of it, the exhibit appears to be the start of the third case in chief of the staff, and not a case limited to the rebuttal of the case put in by the respondent, Colorado Interstate Gas Company. In view of that fact, I submit it is improper rebuttal evidence.

Now, the witness purportedly is now going to talk about the exhibit as a whole, particularly on Schedule A-1 he is going to talk about the effect of the exhibit as a whole, because it is quite clear that that is the summary of all the schedules lying behind Schedule A-1. I believe it definitely goes beyond the scope of a rebuttal case, and I think for that reason we are entitled to know what we are proceeding into, because if the staff again is putting in a case in chief upon which they substantively intend to rely as supporting their own contentions, as countervailing proof against the case in chief put in by Colorado Interstate, we have a very neat procedural question, and I would object to them going ahead on that basis.

It is quite clear that this exhibit is not rebuttal, but this exhibit is the first part of a new case in chief, and lays the groundwork for a subsequent case in chief as is evident from other exhibits which have been served upon the respondent, and this is the fundamental exhibit for that purpose. Consequently, sir, I object to any testimony upon this exhibit.

[fol. 251] Presiding Examiner: I will be glad to hear you, Mr. Goldberg.

Mr. Goldberg: Well, I will tell you, Mr. Examiner, if we were practicing in the 18th Century where we had all this strict pleading that Mr. White is expounding here, I think an answer might be required. This is fundamentally

a rate inqu-ry investigating the company's rates. The Commission is entitled to all the information it can get, including the adjustments which the staff thinks are warranted by Mr. Jones' cost of service study, and that is all that we are proposing to do in this rebuttal testimony.

Presiding Examiner: Now, could I ask you to just interpret that for me? I don't know what the 18th Century has to do with it. I would just like to have that interpreted so I can understand it. His basis of objection is that this testimonzy proposed to be put in is not rebuttal, but is a new case-in-chief. Will you please plead to that now, and let me get the benefit of your advice. The procedural law requires, as I understand the law—and I will be glad to have you advice me on that—that rebuttal be rebuttal. That is your place in this case no-, just as their rebuttal had to be rebuttal. Now, what is this exhibit in relation to their case? That is the question. On the basis of your device, I will try to make my ruling, but let's keep it to what is involved.

Mr. Goldberg: Well, maybe I don't know. They say black is black. I can't say that black is white. I have just got to show that black is not black, not to show what they say is black is white. That, according to your theory is what this situation means.

I say when they come in and show a cost of service study, we can rebut that by showing how that cost of service study would look, considering the Staff adjustments.

Mr. White: Your Honor, that is exactly what the exhibit does not show. It goes much beyond that. It has every iota in here that would be required in a case-in-chief, and rather than meet the case-in-chief of the respondent in this [fol. 252] case, I submit that the apparent purpose of it is to make up certain deficiencies in the second Staff case-in-chief, because I think we might as well note on the record, because it was noted yesterday that exhibits have been served, there is also a cost of service allocation served upon counsel for the respondent. Now, we assume from that they are going to introduce that also, and this Exhibit No. 26 for identification contains that breakdown of material which is necessary to make a cost of service allocation.

Now, it is quite evident that they have not just made their adjustments to the total over-all cost of service put in the case-in-chief of the respondent, but they have gone much beyond that. That was the reason for my inquiry of counsel in the beginning. I wanted to be sure I understood it, because the limited scope of rebuttal certainly doesn't seem to be applicable in this exhibit if it is to go in for the simple reason that it doesn't stay within the scope of the case-in-chief put in by the respondent.

If they are going to attempt to cure what they might think are defects in their own case, that should have been done on redirect examination of their own witnesses, not under the guise of a rebuttal case.

Presiding Examiner: What is the relation of Exhibit 26 to Exhibit 13, Mr. Goldberg, the exhibit put in by Mr. Wiskup before?

Mr. Goldberg: Exhibit 13 was an exhibit on cost of service for three years based on information submitted by Colorado Interstate Gas Company in a certificate application and this exhibit is based on Mr. Jones' exhibit.

Presiding Examiner: Well, does 26 replace 13?

Mr. Goldberg: I don't think the Staff is called upon at this time to make a determination, because we think all this material is relevant, and when we have an opportunity to evaluate the whole record, at that time we will determine what our recommendation will be to the Commission.

[fol. 253] Mr. White: If that is the case, Your Honor, I dare say we would be automatically deprived of due process of law, if they are still putting it in under the guise of a rebuttal case. If it is to be substantively used as evidence in a case-in-chief, we should have the opportunity therefore to put in a case-in-chief in turn. That means we would go on here ad infinitum and never finish.

Presiding Examiner: That is the situation. It boils down, gentlemen, to that very simple thing called due process. If this is a case-in-chief, they have a right to rebut this case-in-chief. Now, do you expect them to have that right? Maybe that will help us. I don't know how many rounds this thing is supposed to take. I am here to serve the needs of justice.

Mr. Goldberg: Well, the point is of course that this is not a case-in-chief. This is just rebuttal, what we say it is.

Presiding Examiner: You say it could substitute for Exhibit 13, yet you leave yourself the alternative.

Mr. Goldberg: According to your view, no rebuttal is testimony, just because it is rebuttal, it is not to be used.

Presiding Examiner: Mr. Goldberg, I am asking questions to try to find out the facts. I am not trying to argue anything. I am asking questions.

Mr. Goldberg: I don't think counsel, or any party should be limited by an- particular type of evidence. The whole record is evidence, and they use whatever part of the record they want, but to limit a party to either case-in-chief evidence, or rebuttal evidence, I think is contrary to due process, to-.

Presiding Examiner: You want me to rule that you can put in another case-in-chief?

Mr. Goldberg: I don't say this is another case-in-chief. I say this is a case in rebuttal.

Presiding Examiner: Do you take the position now that this is solely rebuttal?

Mr. Goldberg: Absolutely.

[fol. 254] Presiding Examiner: And that is does not go beyond the scope of the case put in by Colorado?

Mr. Goldberg: Well, I don't know what you mean by that. All I say is we have taken their exhibit, and made Staff adjustments.

Presiding Examiner: I am trying to find what it is. I don't know a thing about it. I haven't read the exhibits. They weren't served on me. I don't mean to suggest they should have been. Therefore I have got to be governed by the statements you gentlemen make.

On that basis, Mr. White, his representation that this is limited to rebuttal, I think I will have to allow him to proceed. If it shows otherwise, you have remedies.

Mr. White: Very well, sir.

By Mr. Goldberg:

Q. Mr. Wiskup, will you please turn to Schedule A-1 of Exhibit 26?

Mr. White: I understand the testimony will be given here subject to the continuing objection as to no proper rebuttal evidence. I appreciate the fact that Mr. Goldberg has said that it is going to be rebuttal, but my point is that on the face it is not proper rebuttal evidence, and in order to save objection to every question on it, I would like the matter understood.

* * * * * * *

By Mr. Goldberg:

Q. Mr. Wiskup, what did Mr. Jones do as to operating expenses in his Exhibit 21?

A. He listed them in certain groups, as shown in the column entitled "Per Schedule No. 1 of Exhibit 21."

Q. And by reclassifying them, you have just broken them down into other subdivisions, but came out with the same total; is that it, as shown on your reclassification?

A. Mainly the reclassification was bringing together certain groups, that come out to the same total, of course.

Q. He broke them down and you brought them together; is that it?

A. That is the main point involved.

[fol. 255] Mr. White: If your Honor please, I submit that the objection still hasn't been answered, because there is no showing as to the necessity for reclassification as rebuttal of Mr. Jones' Exhibit 21.

Presiding Examiner: We will recess for five minutes at this time.

(Whereupon, at 11:00 o'clock a. m., a recess was taken until 11:25 o'clock a. m.)

Presiding Examiner: Gentlemen, we will recess at this time until 2 o'clock this afternoon, in this room.

(Whereupon, at 11:27 o'clock a. m., a recess was taken until 2:00 o'clock p. m.)

Afternoon Session

(Whereupon, at 2 o'clock p. m., the hearing was resumed, pursuant to the taking of the luncheon recess.)

Presiding Examiner: The hearing is reconvened.

The Examiner called a recess at 11:30 today, after talking with the Chief Examiner by telephone, and with his approval, to permit time for study of the group of proposed exhibits, excepting one—I believe you said there was one more, Mr. Goldberg?

Mr. Goldberg: No, I am afraid not. If I said one more, I gave it to you subsequently.

Presiding Examiner: The last one would be the rates designed by the Staff, is that right?

Mr. Goldberg: Yes, we may not introduce that one. I will have to see as time goes on.

Presiding Examiner: In order that we may avoid, if possible, the necessity of a number of rulings, it seems to me it would be advantageous if we would identify the Staff exhibits at this time so we may refer to them by identification number. Would that be agreeable?

Mr. Goldberg: Exhibit No. 26 has been identified already. [fol. 256] Of course this witness is not going to testify to all these exhibits.

Presiding Examiner: You can still identify the documents.

Mr. Goldberg: The next is a document entitled, "Colorado Interstate Gas Company, Estimated Normal Peak Day, Winter Season 1951-1952 and Estimated 1952 Sales Volumes and Revenues," May that be marked as Exhibit No. 27?

Presiding Examiner: It may be so marked.

(The Document Above Referred to was Marked for Identification as Exhibit No. 27.)

Mr. Goldberg: Next is an exhibit entitled, "Allocation of Cost of Service Based On Estimated Normal Peak Day Winter Season 1951-1952 And Estimated 1952 Sales Volumes and Revenues."

Presiding Examiner: That will be identified as Exhibit No. 28

(The Document above Referred to Was Marked for Identification as Exhibit No. 28.)

Mr. Goldberg: At this time those are all the exhibits I wish to identify, Mr. Examiner.

Presiding Examiner: I have already mentioned the matter of attempting to expedite the orderly conduct and disposition of this proceeding by avoidance, if possible, of a number of rulings of a similar nature, at least presented by similar type of problem.

I believe that that can further be accomplished if we consider ourselves, at the moment, on the basis of a conference between counsel, and with counsel, and I will ask the witness to step down until we have completed this conference, as we will not be taking testimony during this period.

I will also ask the reporter to make an indexing in the [fol. 257] record that this particular number of pages relates to a conference with counsel.

Gentlemen, what I want to do in talking with you is to find the greatest possible mutual understanding so that we may operate as widely as possible on an agreed basis in getting this hearing expeditiously completed.

Suppose I just sort of put before you these facts from the record

As I understand it, you have Exhibits 1 to 18, inclusive, as representing the Staff's case until this session begins.

Mr. Goldberg: Yes, sir.

Presiding Examiner: You then have Exhibits 19 through 23 as being the company's rebuttal case?

Mr. White: That is correct, sir.

Presiding Examiner: That means, then, that the exhibits beginning with 24, to the end of those that have been identified plus another, if there be another later added, represent the Staff's rebuttal case. Is that correct?

Mr. Goldberg: Yes, sir.

Presiding Examiner: I am sure you gentlemen understand and agree that the Examiner has not had an opportunity in the hour's recess, with some time during the lunch period, to make any exhaustive comparison of this material with that which is already of record. The Examiner is quite familiar with the exhibits that precede

Exhibit 24 by reason of the fact that that has been on the record now since some time in December.

I believe that both of you gentlemen will agree with the Examiner's finding from this brief analysis, by no means exhaustive, that the exhibits that *the* proposed to be presented now by the Staff represent in certain respects, at least, that which would be technically referred to as rebuttal testimony. I believe you would both agree to that.

Mr. White: Portions of it, sir, yes.

[fol. 258] Presiding Examiner: I think you would also both agree with the Examiner that in some respects these exhibits contain material which in fact represents a revision of data previously presented by the Staff as their case.

Mr. White: I agree that that is so.

Mr. Goldberg: Well, I would have to check the results of these exhibits with the result of the other exhibits, and frankly I have not done so, because my contention has been that it all goes in one pot, it is all evidence.

Presiding Examiner: I am not talking about one pot, I am talking about the nature. I want to see if you gentlemen agree.

For example, I assume, although it hasn't been stated, that Exhibit 28 would be Mr. French's exhibit, that he would sponsor this exhibit which has been identified as Exhibit No. 28?

Mr. Goldberg: That is quite right, Mr. Examiner.

Presiding Examiner: And I assume that anyone looking at Exhibit 18, and comparing Exhibit 28 to 18 would agree that Exhibit 28 represents a substantial revision of Exhibit 18. It seems to me that one would have to reach that conclusion. Now, that is due not only to difference of treatment, but also to difference of results.

Now, wouldn't you also join us in that general appraisal of that particular matter? All I am trying to do here is to see if you agree with the Examiner that there are both of these elements to a certain extent involved.

Mr. Goldberg: Quite right, but you have also got to include Exhibit 10 of Mr. French.

Presiding Examiner: Yes, I will agree to that, that Exhibit 28 represents a revision of Exhibit 10 and Exhibit 18.

Mr. Goldberg: It doesn't represent a revision, Mr. Ex-

aminer. It is done on the same th ory as Exhibit 10, exactly the same theory, but he used different basic figures because of course the cost of servi in Exhibit 26 is dif- [fol. 259] ferent than the cost of se vice in Exhibit 1.

Presiding Examiner: Well, I had hoped that we could get this much before us. At any rate, that is what I find.

Now, as I say, I don't find all the rest of it, I don't see exactly what part is which, because that is impossible at this stage for anybody to make such a detailed study as to be able to say that page so-and-so line so-and-so, represents either rebuttal or revision.

Now, let's go one step further, gentlemen. If it had been the Staff's desire at a stage prior to the submission of the company's rebuttal case, it could have been possible that the Staff might have seen fit to revise any one of its exhibits, 1 to 18, as a part of their case, a part of their direct case. That would be true, wouldn't it?

Mr. Goldberg: Not revised according to the way they have done it now.

Presiding Examiner: I am not saying that, I am simply saying it could have been done. I find that there are some things that look like revision and I find some things that look like rebuttal. I find both things present. The matter of degree is another matter. We will have to find that as we go along.

Now, the reason I mention the matter of there being some revision, if that revision had taken place before the company put in its rebuttal case, it would have had an opportunity at that time to have rebutted that showing. Is that not correct?

Mr. White: That is correct, sir.

Presiding Examiner: And if there be elements now that represent revision, that they have not in the past been confronted with, would it not be the necessity of fairness that the company have an opportunity to rebut them?

Mr. White: That is absolutely true.

[fol. 260] Mr. Goldberg: What your Honor says is true, if those revisions are any different in principle, but the revisions are not different in principle, and to that extent I don't see what the company has to rebut, because all the revision here has already been testified to by the staff wit-

nesses, or the principles, I will say. All the principles have already been testified to.

Mr. White: That, your Honor, is something that we aren't in a position at this time to say is true or not true. It appears not to be true from the analysis we have been able to make in the short time we have had possession of the exhibits.

I can mention one principle that certainly doesn't seem to be the same, the utilization of a so-called normal peak day.

Presiding Examiner: Of course, as you have already said, it is impossible to determine the minute details. It would seem to me that insofar as the further study of these exhibits make clear upon the record that there is involved, and that these does come about a revision of the staff's showing, which the company has not had an opportunity to meet that fairness requires that they be permitted such an opportunity. I think we can agree in the abstract on that principle.

Mr. White: That is certainly true, sir. The one thing that disturbs me is the gentleman expressed the attitude that that is not the case, and it seems to me that if the staff is putting forth something here as a direct case to which we can't rebut, possibly there is inherent error in admitting it right from the beginning. That is the theory upon which they are offering it, sir. That is my point.

Presiding Examiner: I am going to do this much to alleviate that situation. I am going to say that insofar as it is shown to me on this record that there represents in these exhibits that are pending or will be pending before us—that [fol. 261] is the additional exhibits proposed by the staff—such data as represents an amendment or a revision of the staff's case which the company has not heretofore had an opportunity to rebut that the Examiner will provide that opportunity.

Mr. White: Very well, sir.

Presiding Examiner: I don't think the staff will object to the principles involved, and I hope that the record will be sufficiently clear that the staff will not object to the specific application of it when the time comes. That is done because of basic fairness.

Now, that still leaves the question, gentlemen, for the Examiner, as to the admissibility of that which is both rebuttal and revision.

I would like to state as a tentative thought for the moment, and that which seems to be impelling, and ask that you gentlemen allow me to confront you with it as a tentative thought, that this is an investigation by the Commission, having undertaken the investigation pursuant to statutory powers and duties conceived by the Commission itself to be their duty it seems to me to be underlying a very fundamental characteristic of such a problem that the Commission deserves—and that is why we have these hearings, and that is the ultimate end of these hearings, the purpose of these hearings—that it deserves the very best evidence that it can get. The staff comes forward at this time with these exhibits, and is in effect saying this is our best thinking up to the moment. That is true not only when it is presented in the form of rebuttal, but also should it be in the form of revision of some earlier testimony.

Now, the importance of the Commission's doing justice to both the company and to the public the company serves in the matter of rates is so overriding that my tentative thought is that these exhibits should be accepted upon the basis that in such fashion as they become more than technical rebuttal, they then present the opportunity to the company to rebut the additional testimony, and I have stated that I will give you that opportunity.

[fols. 262-264] Now, that means that in an investigation it appears to me that the overriding importance of the Commision's getting the very best is sufficiently vital that where there is some rebuttal involved, we all admit that, even though there be some revision involved, it must be accepted, and unless we could possibly screen it out, which is impossible to do, then I must admit the whole, and allow you the opportunity to rebut that which is new. Does that seem to you gentlemen wholly fair.

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[fol. 265] WILLIAM F. SPURRIER was recalled as a witness, and having been previously duly sworn, was examined and testified further as follows:

Direct examination.

By Mr. Goldberg:

* * * * * * *

Mr. White: Mr. Spurrier, I believe you have previously testified, have you not, that you are the supervising accounting examiner, or however you may term your capacity, in this G-1115 case?

[fol. 266] The Witness: Yes, sir.

Mr. White: In your discussion of your allocation of costs to gasoline operations, I note that you stated that in reference to what you have called a comparable schedule in Exhibit 1 that Exhibit 1 related to the test year figures whereas your allocation of costs are contained in Exhibit 26 based on the period selected by the company. Do you remember so testifying?

The Witness: Just now, you mean?

Mr. White: Yes, just now.

The Witness: Yes, sir.

Mr. White: As the Staff expert in this case, Mr. Spurrier, would you tell me which period of the various periods that have been shown in this docket you would recommend to the Commission as the test period upon which you would fix rates for the future?

The Witness: Oh, I would recommend that the Commission take the entire situation, that is the results of 1951, June 30, are actual figures. Now, when you move into 1952, as the company did, estimating it for 1952, the only thing the Staff could do was take the same figures that the company did, and apply the same principles that we did in Exhibit 1. Now, I would recommend that the Commission consider both items.

Mr. White: Well, do I understand from that that you would not recommend that the Commission use any specific 12-month period? Was that what you meant to say, sir?

The Witness: Well, I would recommend to the Commission that they use whatever in their opinion they think rep-

resents the best estimate of what the company is going to experience for '52.

Mr. White: Well, then, do I understand that you are not going to recommend any particular period of time?

[fols. 267-282] The Witness: We, personally?

Mr. White: You, as a Staff member and expert in this case.

The Witness: All I am going to recommend is that the Commission consider the results of the actual figures for the test year, June 30, 1951, and the results of the allocation on the basis that we used there, to consider the allocation resulting from using the company's estimates, which fall or stand upon the reliability of the company's own estimates. Now, if they are convinced that those estimates are all wet, then the allocation falls.

Mr. White: I think you are getting beyond the point of making a recommendation. I am asking you what you recommend. Please answer the question. Would you like to have it read again sir?

The Witness: No, I know what you asked. I would recommend that the Commission consider both of them. I am not going to say, "You consider the company's estimate, I think they are the best that there is." I am going to say the results of actual operations, which nobody refutes, would be June 30, 1951, so much. It could very well be that the figures, if they were worked up for the year ended 1951, would show a decidedly different figure. I am going to say to the Commission, "Here is w' we did, here is all the information we had to work with. I can't say, I have no crystal ball to say you take this one.

Mr. White: Then I understand you are not recommending or will not recommend to the Commission any specific period of time, is that correct?

The Witness: As a Staff man, as an individual, I am just going to present the information to the Commission.

* * * * * * *

[fol. 283] By Mr. White:

Q. You recall your unfinished business, Mr. French?

A. Yes, sir.

Q. I had questioned you, as I recall it, in respect to

whether or not you hadn't recognized that administrative and general expenses are not only related to labor and materials, but also to return, depreciation, taxes, and in fact to all costs of service exclusive of administrative and general expenses, and as illustrative of that, I believe I referred you to your Exhibit No. 10 in FPC Docket G-462. Do you recall that sir?

A. I do.

Q. And subsequent to that time, we provided to you a work paper on which we had made a calculation, and which we felt confirmed the fact that you had so treated those items of cost in Exhibit 10 in Docket G-462, isn't that correct, sir?

A. Will you read that question back?

(Question read.)

The Witness: That is correct.

By Mr. White:

Q. Now, are you prepared to answer now, Mr. French, and if so will you please answer, whether or not you [fol. 284] haven't in Exhibit 10, in Docket G-462, recognized the fact that administrative and general expenses are not only related to labor and materials, but also to return, depreciation, taxes and to costs of service exclusive of administrative and general?

Mr. Goldberg: I object, Mr. Examiner. He can ask the witness—if Mr. White wants to ask the witness what he did in that exhibit, that is all right, but to try to get this witness to draw the conclusion is something else, again.

Mr. White: I think it amounts to the same thing.

Presiding Examiner: You mean to say it is wrong to draw a conclusion, why is it wrong? That doesn't give me any basis.

Mr. Goldberg: We don't know what Mr. French did in that exhibit, that is the point.

Presiding Examiner: We are trying to find out.

Mr. Goldberg: He is asking what the conclusion is. I want to find out first what he did. I think the record ought to show what he did. Maybe somebody else would draw a different conclusion.

Mr. White: We asked Mr. French, Your Honor, as to what he had done in that particular document, Exhibit 10 in Docket G-462, and we have not had the answer yet, through no fault of anyone. It is just the fact that Mr. French didn't have the opportunity to check back. He has been given that opportunity, and all I am asking now is an answer to that question.

Presiding Examiner: You may answer.

The Witness: In the original Mississippi case, Docket G-462, I erroneously spread the administrative and general expenses on the basis of all other costs except administrative and general, taking that out, plus some miscellaneous costs classified as "Other."

The Commission in their order caught this error, and in their order this was rectified.

[fol. 285] By Mr. White:

Q. When did you discover this error, Mr. French?

A. Frankly, I didn't know it was in there until you caught it.

Q. Didn't any one of the Commission correct it or call your attention to the fact that you made such an error?

A. I don't remember any discussion on it. I have tried hard to think, but at least I checked the order and opinion as against the exhibit, and find that the order brings it back on the orthodox method.

Mr. White: That is all, your Honor.

Mr. Goldberg: I have redirect on that point, Mr. Examiner.

Redirect examination.

By Mr. Goldberg:

Q. What you are trying to say then, Mr. French, is that that was merely an error in computation, but was not intended to be a method that you recommended at the time.

A. That was 10 years ago. I am positive it was not my feeling of the matter at that time.

Mr. Goldberg: That is all I have.

* * * * * * *

Presiding Examiner: How much time do you think they need?

Mr. Goldberg: I think they need one week. One week is the most they need to prepare for cross-examination. After all, you want to remember that we are looking for a rate reduction, without a bond being filed, and every day's delay is to the benefit of the company.

Presiding Examiner: Maybe; that depends on the ultimate conclusion.

Mr. Goldberg: Quite right, but that is what we are here for, looking for a rate reduction. Don't think we are here to just decide some academic issue.

[fol. 286] Now, I am not accusing counsel of deliberately delaying, but at the same time we can't be naive enough not to know it is to their advantage to get as much delay as they can.

Presiding Examiner: I am not interested in your comments on their motives.

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Presiding Examiner: All right, we will settle on the 8th of April. We will recess until the 8th of April, 1952, in the main hearing room, 1800 Pennsylvania Avenue, N. W., Washington, D. C., at 10 a. m.

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ALEXANDER E. WISKUP was recalled as a witness and, having been previously duly sworn, was examined and testified further as follows:

Cross-examination.

By Mr. White:

* * * * * * *

Q. Is not your justification, set forth on Schedule A-3 of Exhibit 26 for disallowing this particular expense, the fact that you deem it to be non-recurring? Is that correct?

A. That is correct.

Q. Now, would you tell me, Mr. Wiskup, what principle or standard do you apply in determining whether this item is non-recurring or not?

A. It is a cost involved in obtaining approval of the merger before the FPC, and my contention is that once they have the merger approved and do merge that they are not going to have to com- forth for another merger.

Q. Then is it your point, Mr. Wiskup, that the merger is non-recurring?

A. Well, certainly, I believe the merger is non-recurring.

Q. Is it your point also that testimony on the subject of gasoline costing operations is non-recurring?

A. I wouldn't say it is not recurring, but any costs for [fol. 287] such testimony I would say are presumably included in the company estimates for the cost of this G-1115 case.

Q. I am not referring to G-1115 alone, Mr. Wiskup.

A. Well, the cost of that *are* presumably included in the cost of any rate case you estimate the cost for.

Q. Are you sure that is the fact?

A. Do you mean am I sure you included it in the cost of estimates?

Q. That is right.

A. I am sure that the representatives of the company gave a work sheet upon which they purported that all their costs for this case are listed.

Q. I am not talking about this case alone. I am talking about the Commission regulatory expense. That goes beyond this case, does it not, Mr. Wiskup?

A. Do you mean do I think they will have some Commission regulatory expenses beyond this case? My answer is yes.

Q. And are you familiar with the condition of the Commission's order in Docket G-1326 relating to the cost of operating the gasoline plants?

A. I am familiar with a condition in the order, I think it is Opinion 209, regarding the loss in gasoline operations.

Q. Don't you feel in view of that that it might be necessary from time to time for the company to show what is happening with respect to this gasoline plant operation from a cost accounting standpoint?

A. It may be necessary and if it is, the cost of doing that should be included in the estimates of that particular case, where it comes up. That is the estimated cost, if it is an estimate case.

Q. You have sought to make an adjustment here now. I am trying to determine upon what basis you have proceeded. Now, isn't it true that what you did was aside from the fact that the testimony of the gasoline plant costing would not be required in a merger case again, is that right?

A. What I said is that this money applies to the cost of the merger case. They will not have presumably any more merger cases, so they won't have this merger expense in their regulatory commission expense.

[fol. 288] Q. Is there one dollar of merger case expense in the regulatory commission expense claimed by the company, other than this $10,000 paid to Mr. Houlihan?

A. Do you mean on the books?

Q. In the claim of the company in Exhibit 21, and what lies behind it; the company work papers?

A. I don't think the company's work papers identified any as such.

Q. Do you recognize that Mr. Houlihan was an expert witness in the merger case? I assume you do. You testified that he gave testimony on the subject of cost accounting.

A. I know of no record in that case that disqualified him as an expert.

Q. Your purpose in eliminating Mr. Houlihan's fee and expenses wouldn't be because you felt that the elimination was justified because no further testimony of that nature given by Mr. Houlihan would be ever required again, would you?

A. Would you please repeat that?

(The question was read by the reporter.)

The Witness: No, sir.

By Mr. White:

Q. Do you mean that isn't the reason you eliminated it? In other words, you didn't think Mr. Houlihan settled the question for all times?

A. No, I felt that he might be called upon to testify in other proceedings, in which the cost of his testifying and so forth would be included with those proceedings.

Q. Would it have to necessarily be Mr. Houlihan? Couldn't it be another expert witness on that subject who would testify again? Your recognize that, that the company can choose its experts, I hope?

A. Yes, sir.

Q. And is it not a fact, therefore, that you don't know whether or not this particular type of cost may be recurring or not then?

A. I would say it is a merger type of cost and certainly on that basis a merger wouldn't be recurring.

Presiding Examiner: Is the answer really responsive? He is not talking about the merger. He asked you about a type of testimony.

[fol. 289] He has already established that it is a type of testimony that relates to the costing of gasoline in any regulatory matter. After all, a merger case is a regulatory matter too, is it not?

The Witness: Yes, sir.

Presiding Examiner: Then your answer, going back to the merger case, saying that the merger is not going to be repeated, really isn't responsive, is it?

The Commission has a right to your opinion on it. Let us answer these questions.

* * * * * * *

Q. Did you make any study which might enable you to judge whether there is this occurrence of non-recurring items of which we speak, in order that you might determine whether or not an allowance should be made for that?

A. (No response.)

Q. Surely you know, Mr. Wiskup, whether you made such a study, do you not?

A. I studied all the companies' estimates that were submitted to me and all the work papers.

Q. I asked you if you made a study as to the occurrence of non-recurring items. Now did you or did you not?

A. Do you mean as applies specifically to this company for a given period on the books?

Q. Yes. No, it can't be a given period for anything on the books because you have presumed to adjust something because it is non-recurring so you must be projecting your judgment into the future.

Now I am asking you if you have made any study as to the inclusion of an allowance because there is an occurrence or incidence shall we say, year after year, of non-recurring items. Did you make any such study?

A. We studied what had happened on the books in that regard. We studied what the company included in its estimates in that regard.

Q. That is historical, is it not? You were looking at what [fol. 290] happened in the past.

A. I also studied what the company put in its estimates in that regard.

Q. That is what you told me before. I asked you one specific question as to whether you made the type of study to which I refer. I think it is capable of a yes or no answer. If you made it, that is a fact. If you didn't make it, then I want to know about it.

A. I think that in studying the past history on the books, and the projects included in the company estimates, that that study could be defined as a study of the type that you are referring to.

Q. Did you conclude from such a study that there would not be an incidence of non-recurring items in the future?

A. No, I concluded they were amply provided for in the company's estimates.

Q. All right, now let us go to the company's estimates to which you are now referring and you point out to me where there is ample provision therein for the occurrence of Mr. Houlihan or a fee like that of Mr. Houlihan, to testify on the subject of costing gasoline plant operation.

A. I did not eliminate that fee because I felt that testifying on gasoline operations would be non-recurring. I eliminated it because I thought that testifying in the merger would be non-recurring.

Q. That was your sole standard for determining that this was a non-recurring item, is that correct?

A. (No response.)

Q. I think you can tell me what the standard for your elimination was, Mr. Wiskup, without referring to your work papers, can't you? Isn't that possible?

A. It may be possible, Mr. White.

Q. Just a moment. Answer my question, first. Isn't it possible? Don't you know the standards that you applied in determining that this was non-recurring, without referring to your work papers?

A. Yes, sir.

Q. Was that the only standard that you applied?

A. That was the principal standard.

Q. What other subsidiary standards did you apply then, [fol. 291] Mr. Wiskup, and may I ask if you can tell me what they are without referring to your work papers?

A. I considered the historical experience of the company.

Q. Just tell me how the historical experience of the company affected you, so that you decided that this was non-recurring.

Mr. Goldberg: If you want to, you can look at your work papers to determine how the historical experience of the company affected this standard. I think the witness is entitled to look at his work papers on a specific question as to what the facts were in this case.

Mr. White: I am not asking about data or figures, I am asking about principles. Now if his principles are set forth in his work papers, I would be very interested in having him tell us where.

He has told us now that there was a historical experience of the company. He may well have to refer to his work papers. I have no objection to the witness referring to his work papers. I do want an answer to my question and that is why I asked it the way I did.

Presiding Examiner: The witness has the question.

The Witness: May I please have his question.

Presiding Examiner: That is what I meant, did you have it clearly in mind?

The Witness: Oh, no, sir.

(The last question of Mr. White was read.)

The Witness: (No response.)

By Mr. White:

Q. Let me put it this way: Did the fact that the company never had that type of experience before influence you, so far as this subsidiary standard was concerned, as to whether or not this item of expense would be recurring or non-recurring?

A. No, sir.

Q. What, historically, does affect you on this subsidiary standard, in making your determination?

A. The history of the company, with respect to the [fol. 292] amount of regulatory expenses it has had.

Q. How far back did you investigate that regulatory expense, Mr. Wiskup?

A. Without looking at my work papers——

Q. I have no objection to your looking at your work papers with regard to that question.

A. Oh, I am allowed to? Thank you.

Q. You are welcome.

A. I think we went back about three years.

Q. What is the first year you have, Mr. Wiskup?

A. I don't have those particular work papers here.

Q. What type of regulatory expense did the company have of that first year, this three-year period that you went back through?

A. This subsidiary reason, as you call it, was not based on the type of expense.

Q. Was it based on the total dollar amount of expense?

A. Yes, sir.

Q. Well, I think it would be important to determine whether it is recurring or non-recurring, to determine what made up that dollar amount, the specific type of expenditures, don't you, Mr. Wiskup?

A. That was embodied in my first and principal reason, that this was the expense of a merger case.

Q. All right. I want to know what kind of expenses they had back there. You don't know? Is that the answer? Three years ago.

A. I don't recall offhand, sir.

Q. Do you recall what it was two years ago?

A. Not offhand, sir.

Q. One year ago?

A. I don't have those papers, sir.

Q. Is the effect of your testimony, Mr. Wiskup, that what you have attempted to do is to determine what should be normal expenditure, based on the company's experience for regulatory purposes?

A. The subsidiary reason, as you call it, was that the expenses without these merger expenses that the company estimate, were in line with the amount of expenses they had, say on the average, for the period.

[fol. 293] Q. Now, do you recall my question, Mr. Wiskup? Would you like to have it read again? I don't think your answer was responsive.

Presiding Examiner: Read the question.

(The last question of Mr. White was read.)

The Witness: I think I answered the question, Mr. White.

Mr. White: Will you read the answer, Mr. Reporter.

(The answer to the last question of Mr. White was read.)

Mr. White: I submit it isn't responsive. I was trying to establish normalcy from the prior expenditures.

Presiding Examiner: When you don't know what the figures are for the last three years, how do you know whether it is a normal average when you don't know what the figures are? You just said you didn't know.

The Witness: I said I didn't recall offhand. I had those figures at the time.

Presiding Examiner: I don't think you have answered the question. The question is susceptible to a yes or no answer. It doesn't have to be limited with that but it certainly should start with that.

That has been true of about 70 per cent of these questions, lately.

We have been having an interval of about one minute between question and answer. I think the record probably should show that.

I don't think the questions are of such subtlety that they cannot be answered yes or no, and then if you wish to explain, you may, but I do not think we need to have quite the interval between question and answer.

I think we will recess at this time for five minutes.

(Whereupon, at 11:35 a. m. a recess was taken, the hearing reconvening at 11:45 a. m.)

[fol. 294] Presiding Examiner: The hearing will be in order. Before we proceed with the case, I would like to ask the witness to be a little less reluctant.

One of the fundamental bases of the Anglo-American law is that the person presiding evaluate the testimony by reason of the fact that the presiding officer observes the conduct of the witness and the demeanor of the witness. The testimony of Mr. Wiskup during the cross-examination has been characterized by great reluctance. Being a staff witness it seems to me that that is not the attitude that one should take and I would appreciate it if he would perhaps try to be a little less reluctant and answer a little more promptly to obviously possible questions that do not involve long analyses of document.

You may proceed.

* * * * * * *

Q. Is it the effect of your answer that you count on one side those that did go up to court review and on the other side the ones who did not? Is that how you determined it?

A. I think that is the general sense of it.

Q. And what cases did you have in mind when you counted up that didn't go up to court review?

A. (No response.)

* * * * * * *

Q. Now, in making your adjustment to regulatory Commission expense, Mr. Wiskup, the net effect of your adjustment is to reduce the amount which the company claims is proper, isn't that correct, sir?

A. Yes, sir.

Q. And you have not added back in it any items of cost which the company might have made, have you?

A. No, sir.

Q. Did you make any investigation or did you think that there might be some justification for adding in an extra allowance because of estimated expenses the company did not include in its estimate?

A. No, sir.

[fol. 295] Q. Did you feel that your function was confined merely to eliminations?

A. No, I felt that the company would include what they felt were sufficient expenses.

Q. What they felt were sufficient expenses?

A. Yes.

Q. And you felt that your only duty was to inquire as to whether that was too high, in your opinion, is that correct, Mr. Wiskup?

A. I had no reason to——

Q. Now, I asked you what you thought. Now, please answer my question. If you would like to have it read again we will read it.

The Witness: Would you please read it, Mr. Reporter?

(The question was read by the reporter.)

The Witness: No, sir, I don't feel that that is my only duty.

By Mr. White:

Q. What, in addition, do you conceive that you should do?

A. I believe it is my duty to inquire as to whether it is proper or not.

Q. If you would discover, Mr. Wiskup, that in your opinion the company hadn't asked for enough expense allowance whether in this category or not, do you think it would be your duty to make an adjustment upward?

A. If I were to discover that in my opinion that had not included enough, yes, sir.

Q. Have you ever done that?

A. Have I ever discovered any?

Q. Yes.

A. Do you mean in this instant case?

Q. Yes.

A. Yes, sir, I think I have.

Q. What is it?

A. I think on Schedule A-7, particularly the last item, where the company would not allow itself enough average gas plant, I increased it.

Q. You discovered an accounting error there, as a mat-

ter of fact, didn't you? That wasn't strictly an estimate.

A. I discovered what I thought was not a proper allowance.

Q. I am asking you about an estimate now.

[fols. 296-316] Presiding Examiner: Well, the answer was really argumentative, and not responsive. He asked you specifically whether you had discovered an error. That is the question. The question is whether or not it is an error.

Now, you can go ahead and explain it otherwise, if you want.

Mr. Goldberg: Explain what that item is. Don't quibble about it. Explain what it is.

Presiding Examiner: I don't know what the answer should have been, but I know it wasn't responsive to the question.

The Witness: The company simply took an average, a two-year average, instead of a one-year average, for a particular item in gas plant and I felt that they should get a one-year average consistent with what the staff allows in the averaging process and made the adjustments.

Mr. Goldberg: The adjustment increased the average gas plant?

The Witness: Yes, sir.

By Mr. White:

Q. Did you discover any relation to an estimate, rather than an error in the method of handling figures, Mr. Wiskup, in which you increased an expense allowance?

A. An expense allowance?

Q. Yes.

A. No, sir.

* * * * * * *

[fol. 317] BEFORE THE FEDERAL POWER COMMISSION

TRANSCRIPT OF ORAL ARGUMENT

Hearing Room, Federal Power Commission, Hurley-Wright Building, 1800 Pennsylvania Avenue, N. W., Washington, D. C., Monday, June 9, 1952.

The above-entitled matter came on for oral argument, pursuant to notice, at 10:00 o'clock a. m.

Before: Commissioners: Thomas C. Buchanan (Chairman), Dale E. Doty, Claude L. Draper, Nelson Lee Smith, Harrington Wimberly.

[fol. 318] APPEARANCES:

James L. White, Dougherty and White, 30 Rockefeller Plaza, New York, N. Y., and Charles E. McGee, 1729 H Street, N. W., Washington, D. C., appearing on behalf of Colorado Interstate Gas Company.

Jacob Goldberg, appearing on behalf of the Staff of the Federal Power Commission.

The Chairman: Let us be in order.

This matter is before us on a proceeding initiated on the Commission's own motion instituting an investigation under Section 5 of the Natural Gas Act to determine whether any rate collected by Canadian River Gas Company and Colorado Interstate Gas Company subject to the jurisdiction of this Commission is unjust, unreasonable, unduly discriminatory or preferential.

During the course of the proceeding, Colorado Interstate was permitted under the authority of this Commission to acquire the properties of Canadian River so that the present action is confined solely to Colorado Interstate. Following extensive hearings, the Commission by order directed that the intermediate decision procedure be omitted, and set the issues developed by the record for oral argument at this time and place, after the filing of briefs.

Time for oral argument has been allotted as follows:
Commission Staff Counsel, 60 minutes.
Colorado Interstate Gas Company, 60 minutes.
The Commission Staff Counsel may reserve from his opening argument such part of his time as he may indicate for rebuttal.

The reporter is directed to insert in the transcript at this point the Certificate of the Secretary of the Commission with respect to the public notice of this oral argument.

(The certificate of the Secretary, as above-referred to, is as follows):

[fol. 319] FEDERAL POWER COMMISSION

June 3, 1952.

In the Matter of: Colorado Interstate Gas Company, Docket No. G-1115.

Memorandum for the Commission:

The record in the Office of the Secretary shows that oral argument scheduled to commence on June 9, 1952, in the above-entitled matter was published in the Federal Register on May 30, 1952; 17FR; p. 4962, and was sent on May 26, 1952, to the parties and interested persons of record and to States or other governmental authorities deemed to have an official interest in the proceeding.

Leon M. Fuquay, Secretary.

The Chairman: Will counsel enter their appearances in the order designated above?

Mr. Goldberg: Mr. Chairman, for the Staff of the Commission, Jacob Goldberg, Attorney.

The Chairman: And how do you wish to divide your time?

Mr. Goldberg: I shall take 45 minutes for my main argument, and 15 minutes for rebuttal.

Mr. White: For Colorado Interstate, James L. White, Dougherty and White, 30 Rockefeller Plaza, New York;

and Charles E. McGee, 1729 H Street, N. W., Washington, D. C.

The Chairman: You may proceed, Mr. Goldberg.

ORAL ARGUMENT OF JACOB GOLDBERG, ON BEHALF OF THE STAFF OF THE FEDERAL POWER COMMISSION

Mr. Goldberg: May it please the Commission, as has been indicated, this is a proceeding under the Commission's own motion under Section 5 of the Natural Gas Act.

I may say that hearings began on October 1, 1951, and the exhibits that were introduced were pro forma on the basis [fol. 320] of a mergered corporation, so there is no difficulty about the merger of Colorado and Candian River.

The Staff exhibits consisted of a cost of service study based on company operation for a year ending June 30, 1951, and also the Staff introduced an allocation based on that cost of service, a rate of return study, an allocation of the gasoline loss operations, and a full complete rate case.

The allocation at that time showed that excess revenues amounted to $3,272,521.

Thereafter Colorado Interstate raised the question that the facilities authorized at Docket No. G-1326, and the facilities in the pending application at Docket No. G-1677, were not included in the Staff's cost of service study, and Colorado Interstate at that time stated it was expected that these facilities would be in operation during 1952. Accordingly, the Staff then introduced a cost of service study for the future based on the years 1951, '52 and '53, and these estimates were taken from the figures given in the application filed by Colorado Interstate at Docket No. G-1677.

After that, Colorado Interstate came in with a cost of service study in which it, in the main, relied on the estimates in the application at Docket No. G-1677, but broken down. At that time, however, Colorado Interstate did not introduce an allocation, and did not introduce any allocation of gasoline operations, but it introduced a rate of return study.

Following that, the Staff introduced a cost of service study for 1952, based on the estimates which Colorado Interstate had introduced in its case in chief, and thereafter Colorado Interstate introduced another cost of service study for 1952, together with an allocation, and an allocation of gasoline operations, among other things, but those are the highlights.

Now, the Staff does not consider that the amended cost of service study warrants or at least shows any items that are proper costs, so we are relying on the cost of service [fol. 321] study which we introduced following Colorado Interstate's estimates, in which we accepted all their estimates of revenues, their rate base, their accrued depreciation, we accepted their estimates of operating expenses, by and large. There are a few adjustments which I shall refer to. In all, the Staff made six adjustments. Several of course which were introduced in the beginning, which were implicit in this rate hearing, namely the gasoline loss operations, and the depletion for tax purposes.

Now, I shall discuss these six adjustments. Incidentally, the last adjustment has to do with taxes, and that necessarily follows, from any adjustment you make you have got to adjust your tax liability.

Now, the first adjustment is a very simple one. It merely reduced the return from a 6½ per cent rate, which Colorado Interstate had used, to what we then considered a 6 per cent rate of return for illustrative purposes. That deduction was $274,666. Since then, the close of the record, the Staff has recommended a 5¾ per cent rate of return, so that the net result there is $431,061.

There were minor changes in plant account which Colorado Interstate subsequently accepted. There was a minor change in accrued depreciation, or rather in the net plant because of the difference in depreciation for the year, and also a change in working capital because of adjustments in operating expenses.

Commissioner Smith: Mr. Goldberg, does that recommendation of the 5¾ per cent, as contrasted with 6 per cent as a fair rate of return, does that in part reflect your criticisms of the witness Merrill's testimony in respect of rate

of return, and does it involve any question whether in view of the financial costs here shown, management is fully efficient?

[fol. 322] Mr. Goldberg: No, sir, our rate of return, which I shall come to as a separate discussion, if I may——

Commissioner Smith: I thought you were leaving the point.

Mr Goldberg: I am perfectly willing to discuss it now, but I would prefer to discuss the adjustment and then come to that as a separate discussion.

Now the next adjustment was Regulatory Commission Expense. That is divided into three parts. The first part is $10,000, which was paid to Price, Waterhouse for the testimony of Mr. Houlihan in the merger proceedings. That is non-recurring.

In effect, Colorado Interstate states it is non-recurring, but states that a certain cushion has to be allowed for the occurrence of non-recurring items. We maintain that very statement shows it is a synthetic cost, and not a know- cost.

Also, there is an item of $95,000 involving court review of this very proceeding, and we have recommended that that amount be disallowed, because nobody knows what the Commission determination will be in this proceeding, and nobody knows, whatever the Commission determination will be in this proceeding, whether Colorado Interstate will seek Court review.

The third item was the amortization period. Colorado Interstate amortized regulatory commission expense over a three-year period, and we recommend a five-year period. A five-year period is the one usually adopted, and we say there are no unusual circumstances here that warrant a change from the five to the three-year period.

The next adjustment is the annual depreciation and depletion allowance. There has been a great deal of confusion, I am afraid, as to what the staff did in this case, and I think what the staff did is perfectly simple.

[fol. 323] Commissioner Draper: Did they put it on the record, what they did?

Mr. Goldberg: Oh, absolutely.

Commissioner Draper: All right.

Mr. Goldberg: Absolutely. Everything I am saying here this morning is on the record, Mr. Commissioner.

What the staff did in the first go-round, we rolled into depreciation for all the various accounting properties, the Panhandle and Hugoton line were rolled into one composite depreciation rate, and at that point there was very little dollar difference between the annual depreciation that Colorado Interstate claimed, and what we allowed. Part of it was due to the fact that we allowed more for field lines and gathering system than Colorado Interstate claimed because we did it on a unit of production method, rather than straight line of depreciation method.

When it came to the new facilities, the staff felt that this composite rate for the old facilities had already been testified to, had already been cross-examined upon, and the question arose to the service life of the new facilities, and we kept them separate. Now, that is not to say that you can't roll in the whole business, because that is what we did in the first place. We took the service lives of the Panhandle field, the services lives of the the Panhandle properties, and the Hugoton properties, and by the mechanics of weighing them in, dollars, age, and so forth, rolled it in. That is the result here, except we kept it separate to show what we did first, and what we were doing the second time.

Now, in the second—for the new facilities, the staff recommended a 25-year service life. The staff witness explained thoroughly on the record the basis of the 25-year service life, the reserves in the Panhandle and Hugoton fields, the fact that 80 per cent of these facilities were to be used for transmission, and therefore any new gas reserves would necessarily be tied on to the transmission facilities. They are not apt to discard the transmission facilities and build new facilities, but if they get a new field, they will [fol. 324] tie it into the existing transmission facilities.

The fact that Colorado Interstate filed an application to tap the Keyes Field along the route of these new facilities, the fact there is exploratory work in the area, all those facts were explained on the record as to why this witness took a 25 year service life.

Of course, insofar as the facilities are assumed to be in operation as of January 1, 1952, he started to depreciate based on a 4 per - basis as of January 1, 1952.

Now, what did Colorado Interstate do, they work on a diminishing life basis, they take their net plant, and depreciate 1/25th, 1/24th, and when they came to the new facilities, they assigned one twenty first, and one twentieth and a half for those starting during the year. The result of that is they take a service life of only 20 years for the new facilities, and don't show any reason why - take a 20-year service life, except they have started to depreciate on this diminishing life basis beginning January 1, 1948, and just say "We will use the same rate for these facilities," without any reason as to why they are using a shorter service life for these new facilities.

I may say also because the staff has used a different service life than Colorado Interstate, Colorado Interstate says the staff should recompute the accrued depreciation. Well, that isn't so, because the Commission is aware of the fact that the Commission will accept the book reserves, especially where the book reserves have been set up in a rate case, and they have been built up under rates following that rate case, and I need not remind you gentlemen that in 1942 the Commission entered an order fixing the rates of Colorado Interstate, and also fixed the book reserves as of that date.

The fourth adjustment is an adjustment to reflect the loss on the gasoline operations. Now, this entails a discussion of the Commission order in the merger proceed- [fol. 325] ings at Docket No. G-1326. It will be recalled that in the order issuing a certificate in which the merger was approved, the Commission conditioned the approval to provide that the costs properly allocable to the gasoline operations, if they exceeded the amounts that Colorado Interstate would receive from the gasoline operations, then and in that event such excess would not become a part of the cost of service and not be chargeable to the ratepayers in any rate inquiry.

Now, the staff has made a study of the costs properly allocable to the gasoline operations, and have found that

based on a 6 per cent rate of return the loss on gasoline operations is $601,000, and based on a 5¾ per cent rate of return is $585,528.

Now, I may refer, or rather refresh your recollection as to the operations under the merger proceeding. Under the plan which is now operating, Colorado Interstate produces, gathers the liquid hydrocarbons, brings them to the two plants that Colorado Interstate owns and operates, the Bivins plant, and the Fourway plant, processes these hydrocarbons, and delivers them at the loading rack to Southwestern, or Southwestern's nominee, now West-Pan Hydrocarbon. In turn, West-Pan sells the finished gasoline, and in turn transmits 50 per cent to Colorado Interstate, out of which Colorado Interstate has to pay the cost of producing, gathering and extracting the gasoline and hydrocarbons.

Now, as to the Fritch plant, operated by the Natural Gas Pipe Line Company, Colorado Interstate receives certain revenues from Natural Gas Pipe Line—in other words, Natural Gas Pipe Lines takes off some direct costs, and transmits the remainder to the Colorado Interstate. Under the merger agreement, 85 per cent of those revenues received from Natural Gas Pipe Line are transferred to the West-Pan, and only 15 per cent remain with Colorado Interstate.

Now, in making the allocation of the cost of the gasoline operations—and there is no denial that the Commission intended that the gathering cost should be included in [fol. 326] the cost, and Colorado Interstate so admits—the staff used what is known as the relative market value theory.

Commissioner Draper: What theory?

Mr. Goldberg: The relative market value theory, or sometimes called the relative value theory. What they did was this: They took five cents as the cost of the dry gas, and took the estimated revenues received from all the sales, the West-Pan revenues, minus the cost to make it marketable, and those revenues, incidentally, were based on a 5½-cent price for the gasoline, and by weighing them against the relative volumes of gas processed, arrived at a

figure of 18.6 per cent as the total of the wellmouth and gathering cost for the three plants to be allocated to gasoline, and the remainder better than 80 per cent stays with the dry gas.

Now, against that, Colorado Interstate allocates 1.27 per cent of the total wellmouth and gathering cost to the gasoline, and better than 98 per cent to the dry gas, and the reason they arrive at a 1.27 per cent figure is they take one per cent as the shrinkage of the wet gas going into the Bivins and Fourway plant, and 2 per cent as to the gasoline being processed in the Fritch plant, and because of the weighing of the volumes they come out with a 1.27 percentage.

The important thing is that out of total cost of $4,323,547 which Colorado Interstate states is the cost of wellmouth and gathering, only $55,000 is allocated to the gasoline, and I might say that out of $3,852,000 of total wellmouth and gathering cost which the staff found, $715,000 is assigned to the gasoline.

The Chairman: What percentage would that be?

Mr. Goldberg: A little better than 18 per cent, sir. Now as to the gasoline plant, the staff allocated all the cost of the gasoline plant to the gasoline on the theory that the gasoline plants are for the benefit of the gasoline. They did take out a certain amount of cost of plant that is used to dehydrate the gas, and there again there was evidence that in processing the gas through the gasoline plant, it [fol. 327] picks up a certain amount of moisture. That is why the dehydration always is at the tail gate of the plant, rather than at the beginning, because it would be a waste to dehydrate it at the beginning because it would pick up moisture going through the process. Despite that we allocated a certain portion of dehydration cost, or rather all the dehydration cost to the dry gas.

Now, I should say that Colorado Interstate allocates a portion of the gasoline plant to the dry gas, and they do it this way. They say a certain portion, or at least a half of the cost of the gasoline plant are joint costs, and the minute they say it is joint cost, they run into this 1.27 per cent allocation, so in effect they are saying about two-

thirds of the cost, when you include also the cost they assign as direct to the dry gas, in effect they say that two-thirds of the cost of the gasoline plant is to be ascribed to the dry gas, and only one-third to the gasoline extraction.

As a matter of fact, if you take all their wellmouth and gathering costs, and all the gasoline plant costs, and total up all the costs that they assign to the gasoline, you arrive at the fact that only 8 per cent of all these costs is assigned to the gasoline.

Now, we maintain, may it please the Commission, that the relative market value is a more reasonable one, it comports with common sense, it gives due weight to what the parties are investing their money for, the value of the product.

There has been a great deal of literature written on the subject, and from what I have read of it, the relative market value theory is the one that is universally—I say universally, I mean usually, all the writers say the relative market value theory is the one that is universally used in the petroleum industry.

Now, Colorado Interstate also says even if the relative market value theory is the correct theory, the staff has not used the correct market values, and we maintain that we have.

[fol. 328] The five-cent value of the dry gas is much above the weighted average that the Texas Railroad Commission found in the order just preceding the introduction of our evidence.

Commissioner Draper: Where did you get the five cents?

Mr. Goldberg: The Texas Railroad Commission twice a year has hearings, Mr. Draper, as to the weighted average of gas being paid in the Panhandle field, and that study of September of 1951—and this evidence was introduced in October 1951—that evidence showed that the weighted average being paid in the Panhandle field, on the same pressure base that we used, was a little under five cents for the wet gas and dry gas, and we gave them the benefit of the doubt and used five cents for the dry gas.

Now, also, Texas has a production tax as well as a gathering tax. It had a production tax for a long time. Under

the production tax, the producer has to pay a tax based on the market value of the gas and in paying that tax, Colorado Interstate, or rather Canadian River, used a value of 4.33 cents for the gas. That was what they said was the market value of the gas.

Also, as I will come to in a moment, we used a five-cent allowance for depletion purposes, and we felt to be consistent if we were going to use the five cents for tax purposes, we should use the same five-cent value for this allocation, and also, so far as this relative market value and shrinkage theory is concerned, when Colorado Interstate pays special royalties for the gasoline content, there are some contracts where there is a special allowance for the royalty for the gasoline content, they don't pay the royalties based on shrinkage, they pay them on the gross revenues received at the tail gate of the gasoline plant. That is what the royalties are based on, on the value.

The fifth adjustment has to do with depletion allowances for tax purposes, and I refer to the Commission opinion in Docket G-1326. I think you gentlemen will recall that Colorado Interstate, in support of the public convenience and necessity for the merger alleged that the benefit that Colo- [fol. 329] rado Interstate would receive from the merger would be the five-cent depletion allowance, and when it was pointed out that the last settlement with the Internal Revenue for the 1945 tax year was based on a 3.17 cents depletion allowance, Colorado Interstate said, "Oh, no, we are going to get the five-cent allowance." Based on that—and I need not quote the Commission, it is in the order—they found that it was reasonable to assume that the five-cent value would be allowed, and all the evidence in Docket G-1326, all of which evidence was incorporated by reference in this proceeding, there has been no new fact to show any change of condition, nothing, and we maintain that Colorado Interstate is estopped, for one thing, now, to say that the rate should be fixed on the 3.17 cent allowance for tax purposes as against the five-cent rate. The Commission was led to believe that the five-cent rate would be proper——

Commissioner Draper: Well, we are dealing with facts

here, suppose we presume it is five cents. Should we adhere to the 3.17, or what should we do?

Mr. Goldberg: We took a five-cent value, because that is what they said they would get. They are claiming more than 3.17 now, and have been since the merger proceedings.

Commissioner Smith: How much time intervened between the representation made in the merger case, and the presentation of evidence in the rate case?

Mr. Goldberg: I will say this much. The merger hearing was concluded, the order was issued in February 1951. Now, certainly if they knew of any facts that would disprove the five-cent rate, I think they were duty-bound to inform the Commission.

Commissioner Smith: It would seem so to me. I take it your position is if the contention is made in one direction in one case, then that contention should not be departed from five minutes later for purposes of another case. Is that your position?

[fol. 330] Mr. Goldberg: Well, not as *bald* as that. I do say this, however, Mr. Commissioner. Where they make a representation on which they expect the Commission to rely, and on which public convenience and necessity is the basis of the representation, the Commission relies on that representation, issues the certificate, then in those circumstances I don't think it lies in their mouth to turn around and say they want the 3.17-cent rate for tax purposes. Not only that, but in April 1951, after notice of this hearing went out, you will recall notice of this hearing went out in March of 1951, or at least it was intimated in the order of the merger proceedings that the Commission intended to set the rate matter for hearing. The order went out in March. In April of 1951, they filed application in Docket G-1677, and at that time in their pro forma estimate of expenses, operating expenses, they used a five-cent rate for tax purposes, for the depletion allowance.

Not only on the theory of estopped, but on the theory there are no new facts here, aside from the time, if there were any new facts within the period of time, they introduced none at the hearing, and we maintain they couldn't

introduce any, there were none to our knowledge, so based on the same facts they intended the Commission should rely on for the five-cent rate, they should rely on the same facts in this hearing.

Now, the sixth adjustment has to do with taxes. There is nothing to discuss there, because they follow automatically from the other adjustments.

I want to say a word about the amended cost of service that Colorado Interstate introduced. What they did, they took their January payroll figures for general and administrative, added 4 per cent to that, and multiplied it by 12 and came out with an annual payroll. They increased that amount by $165,000.

The four per cent increase, of course, is synthetic. That is something that they expect the cost to increase by that amount, and we show as of the date when they introduced that, the cost of service actually was declining.

[fol. 331] The other operating labor they increased by 8 per cent, 4 per cent of which they say——

Commissioner Wimberly: You say the operating costs were declining. Are you referring to payroll cost?

Mr. Goldberg: I said the Department of Labor Monthly Statistics declined. They said 4 per cent increase because of future cost of living increases. They are not paying that 4 per cent, but they said there may be some future cost of living increases. We showed that at the same time they were saying the cost of living was going to increase, we introduced the Department of Labor statistics showing a decrease, and the other operating labor they increased by 8 per cent, 4 per cent they say they are actually paying, and 4 per cent is future increase in cost of living.

We maintain that so far as the actual 4 per cent, that has already been taken care of because there are a lot of future operating expenses in these estimates. Nobody knows what will happen——

Commissioner Wimberly: In making their estimates, they included figures for increased costs?

Mr. Goldberg: Yes, sir, for more employees.

Commissioner Wimberly: And then added another 4 per cent?

Mr. Goldberg: On that, another 4 per cent. Now, we allowed all the future employees they said they would hire. We made no adjustment downward because somebody might leave a job and they wouldn't fill the job. We made no allowance for the fact that as a result of the merger certain economies would result: office rent, office machines, and so forth.

Now, the other costs are the gas royalty expense they say they will incur, those were not actually known costs.

We included everything they were paying. These were things they said they might possibly have to pay, except one (fol. 332) item, the directors and executive committee payments. Apparently they will pay that because that was voted on at a board of directors meeting. I need not go into the details of that, it is explained in my brief.

In March, just before the public offering of the stock, the two largest stockholders, the Union Securities group, and the Sinclair [illegible]orporation, the presidents of each became directors, and also members of the executive committee, and they voted themselves a $5,000 fee as director, and a $30,000 fee for Mr. King, president of Union Securities, and $15,000 fee to Mr. Spencer of Sinclair.

Commissioner Wimberly: $15,000 annually?

Mr. Goldberg: In addition to the five, and then in the next month those corporations were going to sell their stock to the public, and we maintain prior thereto the directors never got fees as such, they got expenses, and the executive committee never got fees, as such. There was nothing in the record to show what these people were going to do. The circumstances surrounding the voting of these payments we felt showed they were not proper costs of service.

The Chairman: You seem to relate these new fees to the sale of stock. What is the relationship there, or is there any?

Mr. Goldberg: Well, I say within a month. It was less than a month, within three weeks after this Board of Directors meeting, the Union Securities group was going to sell most of its shares, and Sinclair was going to sell all of its shares, and yet the President of Sinclair becomes one of the remaining Board of Directors, and Executive Commit-

tee, and Mr. King remains as one of the remaining directors, and also Chairman of the Executive Committee, and it just seems to us the whole circumstance showed a clear-case of feather-bedding.

Commissioner Smith: In effect, you are contending this is a kind of lame-duck action, which resulted in a sort of feather-bedding?

Mr. Goldberg: Yes, sir.

[fol. 333] Commissioner Smith: You spoke of the circumstances. Does the record show the circumstances of the directors meeting?

Mr. Goldberg: Yes, sir. I couldn't get into it too thoroughly, but it shows the dates, the sequence, who the people are, and the fact of the public offering.

Commissioner Smith: Does it show the voting of the respective directors?

Mr. Goldberg: I tried to get that, but couldn't, Mr. Smith.

Commissioner Smith: You mean the information was refused?

Mr. Goldberg: Well, the Examiner ruled, as I remember his ruling, that so long as the Board of Directors voted on that, we could not ask the witness who sponsored the cost of service, and who stated that all of these costs were proper costs of service, we could not cross-examine that witness on that line, and at that time I was stymied, despite the fact that I tried to get—the witness admitted he was sponsoring all these as proper costs of service, the Examiner felt that the Board of Directors having voted, it was an ipse dixit transaction.

Now, I understand that Mr. Spencer has refused to take the $15,000. You can draw any conclusion from that that you want, gentlemen. At any rate, it is not a cost of service, if they are not going to pay it to him.

Commissioner Draper: Maybe he doesn't need the money.

Mr. Goldberg: It may be because of his income tax.

The Chairman: But he did refuse the $5,000 directors' salary?

Mr. Goldberg: I think so. As I read it, he is going to resign from the whole Colorado Interstate situation. He hasn't done it yet, that I know of.

Commissioner Smith: Let me see if I understand your position here. You are not necessarily, as I understand your position, you are not necessarily objecting to proper [fol. 334] payments to what you might call public directors for services which they may have to render in connection with the responsibilities that they assume, but you are pointing here to the fact that these are not public directors in the usual sense, these represented institutional investors, or controlling companies, or financial institutions.

Mr. Goldberg: Quite right.

Commissioner Smith: Mr. King is who?

Mr. Goldberg: President of Union Securities Corporation, which is in turn a subsidiary of Tri-Continental, another holding company.

Commissioner Smith: Well, I am not interested in that, but Union Securities, you said they were disposing of their ownership interests, in large part, at least, in Colorado Interstate.

Mr. Goldberg: Yes, sir.

Commissioner Smith: Well, now, does what you say Mr. King's position is——

Mr. Goldberg: He is president of Union Securities.

Commissioner Smith: I mean his position with Colorado Interstate.

Mr. Goldberg: Director, and Chairman of the Executive Commmittee.

Commissioner Smith: And as Chairman of the Executive Committee, would he be in a particularly advantageous position in so far as acquiring the financing of Colorado Interstate is concerned in the future?

Mr. Goldberg: I don't think he would be in any more favorable position than anyone else so far as helping Colorado Interstate's financing.

[fol. 335] Commissioner Smith: I wasn't talking about that, I was talking about securing that business for his own concern, Union Securities.

Mr. Goldberg: Oh, yes, sir.

Commissioner Smith: Does the record show whether Union Securities participates in pipe line financing?

Mr. Goldberg: This record doesn't show it, no, sir.

Commissioner Wimberly: Is Union Securities a financing house?

Mr. Goldberg: Yes, sir, and I think it is common knowledge that they financed Mississippi River Fuel, and some others.

Commissioner Smith: Mississippi River Fuel, did you say?

Mr. Goldberg: Yes, I am pretty sure about that.

Commissioner Smith: Didn't the president of the Mississippi Fuel recently go on the Board of Colorado Interstate?

Mr. Goldberg: Quite right.

The Chairman: That was at the same time, was it not?

Mr. Goldberg: Yes, sir.

The Chairman: Did you say Union Securities was the agencies for the sale of stock?

Mr. Goldberg: Yes, sir, for the public offering.

The Chairman: In response to Commissioner Smith's question, there was relationship, then.

Mr. Goldberg: As a matter of fact they got quite a fee for handling the sale of the public securities.

Commissioner Wimberly: Just a minute. Was any additional stock sold to the public other than that which was owned by Sinclair, and by Union Securities?

Mr. Goldberg: Largely those two. I think there was a [fol. 336] small amount that some private people sold, but whatever it was, it was so small it was lost in the shuffle.

There is one other point about the pension benefits, and so forth. Now, we allowed every cost for pension and group hospitalization, but they came in with their amended cost of service and said one insurance company had submitted a new plan which would increase the cost. The Board of Directors hadn't even considered that plan, and we rejected it.

The Chairman: Are there any representatives of that insurance company on this Board?

Mr. Goldberg: Well, the insurance company happened to be Prudential. All I can say is that Prudential Life Insurance Company owns most of the notes of Colorado Interstate, but this was one plan by one insurance company, the Board of Directors hadn't even considered it, and we felt

in view of that it was not a known cost that should be allowed in cost of service, but we did allow every cost they are actually incurring for the payment of pensions and hospitalization.

Now, classification and allocation will take just a moment. The recent Atlantic Seaboard case, we think, is determinative of this case, and dispells the allocation classification that Colorado Interstate made. Every known cost they could consider fixed was classified as a fixed cost, and thereby transmitted into a demand cost.

As to rate of return, we feel that this is a very unusual case, and that the Commission here has concrete evidence as to what the cost of equity capital is. I may say that the cost of debt financing, and preferred stock financing, there is no dispute between the Staff and the company, that we come to the cost of equity capital, and you couldn't have a better case. Two days before the hearing closed, they sold to the public 966,000 shares of stock, Union Securities group, and the Sinclair group, and they sold them to the public at $26.75, net to the sellers, $25.25.

Based on the $1.88 earnings as of December 31, 1951, on earnings price ratio, it is 7 per cent. If you want it on the net company price ratio, it is 7.5 per cent.

[fol. 337] Now, I can't see what better evidence you want of what the cost of equity money is when two days before the hearing closed, they sold 56 per cent of the outstanding shares to the public, at a cost of 7 per cent, and we allowed almost 9 per cent, 8.95 per cent, so certainly the Staff was generous in allowing 9 per cent, or almost 9 per cent as against the 7 per cent it actually cost them.

Their financial expert, Merrill, said the cost of equity capital should be 11 per cent, and he based it on certain earnings price ratios he picked out, and came out to 11 per cent. The staff of course also used earnings company price ratios based on the monthly averages of the natural gas stocks that are traded on the New York Stock Exchange. We took the monthly average of the seven natural gas com-anies who report to the Commission, and that averaged out at 8 per cent on an earnings price ratio, and we allowed 8.95 per cent.

The Staff feels that 5¾ per cent over-all rate of return is generous to the company, and I might say that had we stayed with the 7 per cent, or the 7.5 per cent as the cost of equity money, the over-all rate would have been something like 5⅛ per cent rate of return.

I don't know whether you gentlemen are interested in the results of that financing, but unfortunately the hearing closed before the results became known, but Colorado Interstate has filed a post-effective amendment No. 1 to their registration statement, which is already incorporated in these proceedings, and I should like to move that that post-effective amendment No. 1 of the registration statement be incorporated by reference in this proceeding.

Mr. White: I have no objection, Mr. Chairman.

The Chairman: We will take the matter under advisement.

Mr. Goldberg: I should like to disclose, however, that they oversold their shares, and the result is they have got [fol. 338] to buy back on the open market, or buy back from Sinclair some remaining shares at a price higher than what they sold to the public.

Commisioner Smith: Who is they?

Mr. Goldberg: The sellers, the Union Securities Group, the head of the underwriters. Now, we maintain, may it please the Commission, that the cost of service proposed by the Staff, and the allocations are just as reasonable, and should be accepted by the Commission. Thank you.

The Chairman: We will recess for five minutes.

(Whereupon, at 10:52 a. m., a recess was taken until 10:57 a. m.)

The Chairman: Mr. White?

Oral Argument of James L. White, on Behalf of Colorado Interstate Gas Company

Mr. White: May it please the Commission, as indicated by Staff counsel, the differences between the company and the Staff at this point in the case relates to rate of return, depreciation, the cost of gasoline plant operations, income taxes, particularly the wellhead value percentage deple-

tion, and certain adjustments to cost of service, as well as the allocation of cost as to which there are fundamental differences, but the allocation of cost - always be dependent first on the cost of service which you allocate, the main stress has been placed and will be placed by me upon the cost of service itself.

Commissioner Draper: In dollars, what is the difference between the Staff?

Mr. White: Between the Staff and the company, Mr. Commissioner, it is roughly about $4,000,000.

Commissioner Wimberly: That is the over-all difference?

Mr. White: The over-all difference, yes. In our principal brief, page 3, starting at page 3, we indicate the various [fol. 339] costs of service which the Staff had put in, and they indicate an overall excess of $3,296,000 on their last cost of service, the year 1952, which upon allocation amounts to $3,077,365, and the company indicates a deficiency applicable to jurisdictional sales in the amount of $1,837,000.

The over-all deficiency is $838,819, in the company's presentation, Exhibit 30 in this case.

Now, on the matter of rate of return, the principles under which this Commission must act, and will act, have been set forth in the famous Bluefield Water Works case, and more lately in the Supreme Court opinion in the Hope Natural Gas Company case. The principle upon which you are to proceed is that the financial soundness of the business must be assured, and the return to the equity owners should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover—and I am quoting the Supreme Court Hope case now—should be sufficient to insure confidence in the financial integrity of the enterprise so as to maintain its credit, and to attract capital.

It is our contention that the application of that principle here requires a minimum rate of return of 6½ per cent. You must bear in mind that all companies, all industries regulated and non-regulated, compete for the investor's dollar, and the investor is a fellow who can look at things pretty objectively and find what offers him the best rate of return.

As Mr. Goldberg says the greatest difference between the Staff and the company on the rate of return presentation is the requirement of the return on the common equity. Mr. Goldberg made reference to the fact that the stock had been sold just two days before the conclusion of the hearings in this rate case, a substantial block of the company's stock. I must point out that the company did not get any new money out of that stock. That wasn't the company's stock that was being sold.

[fol. 340] Commissioner Smith: What has that to do with it? That nevertheless represented the independent investors' market appraisal of the worth of the stock?

Mr. White: I wonder if it does.

Commissioner Smith: I don't know how you could get a better test.

Mr. White: Mr. Commissioner, there is this to it. You must remember in effect there was being a liquidation of certain interests which had previously held Colorado Interstate Gas Company, and it was pursuant in part to an order of the Securities and Exchange Commission. Now, the company had been newly merged, only as of the first of this year, and investors may be willing under those circumstances to take a smaller yield where there is a greater dependence upon developing earning power as in effect a new enterprise proceeds, which is the fact here. This is the first time the company has operated as an integrated company.

Commissioner Smith: I recognize the force of what you say, but notwithstanding the fact that this was in a sense a forced sale, the fact that there was, at least so Mr. Goldberg asserted, over subscription, it looks as though not only is your company competing for the investor's dollar, but the investors were competing for your company's securities at this price.

Mr. White: That appears to be the case, and there is no gainsaying the fact that there was an oversubscription of it, but there are these other factors which must be borne in mind. Were the company itself in a position of acquiring funds, then the investors' appraisal might be a different one entirely.

Coming again to the Bluefield and the Hope principles on

that, we have got to look at what must be given from the competitive standpoint so we effectively can compete for this investor's dollar, and it is on this basis that we contend that the return on this equity hadn't been the 8.95 [fol. 341] per cent which Staff counsel is contending for, but must be 11 per cent.

Now, as to the 8.95 per cent which the Staff has put forth, the Staff in effect—I think its brief clearly indicates this point—has decided 5¾ per cent is an adequate return to Colorado Interstate Gas Company, and from that they determine that 8.95 per cent return would result on the common equity.

Now, we have replied to that at some length, and I am not going to quote from the brief, in any respect. I am confident that the Commission will read the briefs in this case, but I do, for the purposes outlined, want to follow what we say there in relation to this 8.95 per cent which the Staff contends is adequate.

In arriving at this, the Staff has eliminated from schedules in their rate of return exhibit anything that is higher than 8½ per cent yield on common equity. In effect, what they do is eliminate items, six in number—I am sorry, what I mean to say is if they are going to effectively determine what is an investor's appraisal of the requirements of return upon equity money, they should eliminate any items that are those of companies that have as yet undeveloped earning power.

Now, in the schedule which they assume to use as support for this 8.95 percent, there are six issues of the Tennessee Gas Transmission Company which it is shown in this record has not developed its earning power, and similarly the case of Texas Eastern Transmission Corporation, two issues of Texas Gas Transmission Corporation, MidSouth Gas Company, which is probably the baby of all the gas companies right at the moment, Equitable Gas Company because there again there was not an offer for new money, it was a great deal in the situation of Colorado Interstate, it was being sloughed off as a part of a previous holding company system, and we contend that out of a list of 25, only seven of the 18 used by the Staff—they didn't use 25, they used

18— are left, and if we take the yield requirements on those common stocks we find that we come up not with 8.95 per [fol. 342] cent, but rather with 9.8 per cent.

Commissioner Smith: You are saying, as I understand it, that there should have been eliminated those companies to which you referred because their full earning power had not yet been developed.

Mr. White: That is correct.

Commissioner Smith: I thought in terms of your answer to my earlier question, you contend those are the very companies that should be taken into account, because comparable to your own situation.

Mr. White: I don't mean to indicate that, sir. I am indicating only this, both with relation to the recent sale of Colorado Interstate's stock, and the companies to which I was just referring, that someone is willing to take less now when he expects more in the future as the company develops.

Commissioner Smith: I understand your point, I think.

Mr. White: I think that is the case here.

Now, in developing the contention that 11 per cent is the return we should have on our common equity stock, I want to discuss just how this was approached by the witness Merrill, Colorado Interstate's witness. He noted the position of the natural gas industry in the over-all economic picture, and one of his prime sources of material on that was this Commission's statistics of natural gas companies, and he noted there the tremendous uptrend in gas sales which has been going on for some time, and he noted comparative profit trends, and he compared the trend of the net income of natural gas companies, as shown by the Commission's statistics, with the trend of the net income of 20 leading oil producers and refining companies, and with about 350, or 378, I think, to be exact, industrial companies.

[fol. 343] Now, the results of this study showed that from 1946 to 1950, profits of the oil industry increased 116 per cent. The profits of the industrial group increased 100 per cent, while the profits of natural gas industry fell behind both of these groups, and increased only 78 per cent

above the 1946 level. At the same time the gas sales had increased far and beyond any of these comparable industries so far as their gross output was concerned.

Now, reducing that to percentages, for comparative purposes, the average return by representative oil companies showed an increase of from 6.52 per cent to 12.92 per cent between the three pre-war years 1939 to 1941, and in the five post-war years, 1946-1950. Manufacturing companies showed an increase from 9.40 per cent to 14.5 per cent during those two different periods. The average rate earning power of natural gas companies, however, was 6.82 per cent in the pre-war years, and only 7.04 per cent for the five post-war years. Now, we just aren't keeping up with the general economy on that basis, so then he analyzed the composition of the invested capital in these various industries, and he found that the natural gas industry from 1939 through 1950, the long-term debt to total capitalization rose from 35.4 per cent since the end of the war to 54.3 per cent in 1950, and the period January 1, 1946, the total increases in invested capital was $2,228,000,000, of which $1,506,000,000, or 67.6 per cent was raised by debt financing. Contrasted with this the oil industry, which we conceive of as being comparable, it is an extractive industry engaged in developing a wasting asset, they raised substantially all their new capital without very significant changes in long-term debt, about 85 per cent of their new money being secured in that way.

Now, the purpose of pointing all this out is that you have got to realize that one of two things is happening. Either the companies just like to finance through debt, which I don't think is true, or else they have got to preserve a reasonable earning for the common stockholder by having equity thinned out, or, as we sometimes refer to it, highly levered.

[fol. 344] Now, the cost of debt money, the composite company cost is 3.21 per cent. The latest cost of debt money to the company, however, as the Commission knows, is 3.75 per cent, and that was the most recent loan from Prudential Insurance Company, the loan agreement itself antedating the merger of the two companies. The industrywide requirements seem to be 3.50 per cent. The cost

of debt money has increased over the years. It seems particularly to have increased since the early spring of 1951 when the Government withdrew its support of Government bonds.

On preferred stock, the situation isn't very important, but the company does have a small amount of preferred stock and as the Commission will note from Exhibit 43, I think it is, in this case, it is contemplated that that could be retired. It will have to be retired either through replacement by more debt money to be able to retire it, or it will have to be replaced with common stock issuing, in either of which case the effect would be, if it were done through further debt financing, while the effect of the preferred stock on the over-all return picture here would be lessened, you would still have at least 3¾ per cent to be earned on that money, or, if you replaced it with common stock, as we contend, 11 per cent is required.

The evidence in this case, I am confident, shows if you will take those instances, those companies which are putting out common stock issues, if you take the evidence in this record, and I think any place where it is available, the common stockholder is going to require more than 8.95 per cent. There is no question that the common stock has always required a higher return than anything else. There is no question about the fact that if you take an objective appraisal of it to come below the 11 per cent is just not going to give the common stockholder enough to warrant his attention.

I have touched upon this matter in the discussion of the rate of return. In 1945, the Mississippi River Fuel rate case, the first rate case, I have reason to remember, the [fol. 345] rate of return was reduced from 6½ to 6 per cent.

The statistics which I have just noted, when you are comparing the trends of natural gas financing with the trends in financing of other companies, particularly in this period since the time of the Mississippi River Fuel decision reducing the rate from 6½ to 6, we will see the great influx of heavy debt financing by the natural gas companies. Exhibit 19 in this case contains some very illustrative charts showing in columnar form just how that is building

up, greatly ahead of other industries which have remained practically the same in their ratio of debt to equity financing.

It seems to me that there must be more encouragement given, there must be more thought given to allowing a company some encouragement for doing more equity financing. The fixed charges that result from heavy debt financing, the companies in the natural gas industry could well end up in somewhat the same position as the railroad industry did. We know what happened there because of the heavy debt financing.

Commissioner Smith: That wouldn't be so likely in this field where you have for the most part serial maturities with sinking funds which were lacking in the case of rail bonds?

Mr. White: The serial maturities and sinking funds' requirements still require a heavy drain upon the company's cash as it is earned, and you won't find——

Commissioner Smith: It also provides for the extinguishment of the debt.

Mr. White: That is true, but at the same time there is hardly any difference if you are going to have to spend too much money to meet the fixed cost of debt, including serial retirements over a 10-year period, or have to meet it at the end of that 10-year period, if you are going to be embarrassed every year, or every time you have to meet serial retirements.

Commissioner Smith: Suppose we were to agree with you [fol. 346] in the contention you have just made, could we require the conversion of debt into equity in the case of your company, absent new construction requiring a certificate?

Mr. White: I am sorry, sir, I didn't hear the last part.

Commissioner Smith: If we were to agree with your last contention, could we then require the conversion of your debt into equity securities, absent any certificate proceedings?

Mr. White: I don't think so, sir. The company will certainly be financing in the future, and so will others.

I might say the matter of greatest difference between the Staff and the company relates to Federal income taxes.

The sole issue I am going to discuss on Federal income taxes relates to the wellhead value for percentage depletion. I might say there is no question that the company estimated in the merger case and fully intended to get a five-cent wellhead value for percentage depletion purposes. We are certainly still firm in our purpose that that is exactly what we want to do.

The question is, since you are in a position now where, if it is found that we are charging too much, if there are excessive revenues, in other words, you will take actual cash away from us in the sense that you will not permit us to earn those excess revenues, there is a great question as to exactly what to do between now and the time the company can realize that depletion value if it ever does.

Now, this Commission has recognized in the merger case it has no control over this wellhead value. You stated in the majority opinion there, as I recall it, that you do not, and do not seek to control the Bureau of Internal Revenue in whatever it may decide is proper wellhead value for percentage depletion purposes.

I think there were even stronger opinions in the dissenting opinion. The majority said these things can't be forecast with exactness. We don't know what the wellhead value is going to be. We think that based on what would [fol. 347] appear to be reasonable, five cents seemed to be reasonable to us, then we don't know whether it is going to be four cents, it might be six cents. I hope it is. But the fact is that when you are in a rate proceeding, where the actual dollars will not be permitted to be earned by the company if you use a smaller income tax allowance because of a higher wellhead value, then I think we must pause before we decide what the company can do, and what can be asked of the company to do.

Now, your Honors may be interested in what the company has been doing. There hasn't been much time since this merger was accomplished, and if your Honors would care to do so, I can bring you up to date on what has been done, which is not in the record. I have the company treasurer here, and could put him on the witness stand if that would help complete the record, but there has been this. The company has asked the Bureau of Internal

Revenue for a ruling on what that wellhead value would be. Last week, in pursuance of that, there was a conference held with the man in charge of the natural resources section of the Bureau of Internal Revenue, and he stated at that time that while they appreciated this company's problems—we acquainted them with the rate situation, we said this is important to us, we have got to know it, it is important to the Power Commission, and is important to the public. He stated it is the settled policy of the Bureau of Internal Revenue not to issue rulings which are necessarily factual before the facts are available, and he said for the year 1952, those facts will not be available before the end of the year 1952.

The Chairman: That is the same explanation we got in the merger case back in 1950, almost identical.

Mr. White: I think that is correct, sir, yes.

The Chairman: So it is just a continuing process.

Mr. White: You are always behind on income tax.

The Chairman: You are always hopeful?

[fol. 348] Mr. White: Oh, yes, we certainly are, but we want to be hopeful with the money, too, and the thing here is we ask if there is some formula that we can make a more intelligent estimate on, because this is a matter of importance to us, he had no such formula to offer. We asked then if we could go to the field engineer and have him work on it in advance, and he said that can't be done, so the fact is until the actual year's taxes, the returns are filed and the Bureau of Internal Revenue knows what their determination is going to be, and it may have to go to court review, and we would certainly take it up there to try to get the wellhead value, this company can't know what it stands to lose on the actual wellhead value, and it may be more than a million dollars a year until that particular situation is met. Make no mistake about it, we want that higher wellhead value. It would be a mistake for us not to try to get it, but with the interposition of another agency, such as the Bureau of Internal Revenue, and with those very practical situations, I submit to the Commission it would be unrealistic to knock us down on federal income tax allowance until there was something definite to go on.

If it would please your Honors, I would be willing to

give the reporter a copy of the letter with the request for ruling, if you would care to have it copied into the record.

The Chairman: I don't believe we do.

Mr. White: On the matter of costing gasoline operations, as Mr. Goldberg has already pointed out, the staff used what purported to be a relative market value method. This, again, is a matter which was discussed at some length in the merger case, and I believe that the Commissioners are familiar with how it operates.

We contend that the relative market value method is, in itself, an unsound one, an economically unsound one. While we recognize it is popular in a good many places, particularly in refining of petroleum products, it is used there as an expedient because there seems to be no other way they can attempt to cost things, it is one which by its own terms falls if the two joint products that you are trying [fol. 349] to price are of different stabilities.

We have here, for one thing, a stable natural gas price, and a gasoline price which is subject to very extreme fluctuations. Exhibit 31 in this case indicates they fluctuated in the last seven years more than 800 per cent.

Now, if you have enough variation, you will find that you are making money on the products today, doing exactly the same thing to it tomorrow, but losing money. That, to me, does not indicate an economically sound approach to costing joint products.

Commissioner Smith: Is your objection based on the view that you don't have true joint cost production when you can vary the relationships between the simultaneously produced products?

Mr. White: Do I understand you to mean, Commissioner, that you may control the output of each of the two products, that you can cut down on the production of gasoline?

Commissioner Smith: Yes.

Mr. White: I think there is definitely something to that, because they are not too necessarily joint products, you can say.

Commissioner Smith: That might be a theoretical objection to the use of the method.

Mr. White: As a matter of fact, under the terms of the operating agreements, the memorandum stipulations which

preceded the merger, which is a part of the record in this case, the Colorado Interstate Gas Company, in cases of necessity, can by-pass the gasoline plant and shoot wet gas up until such point where as a practical operating matter it starts clogging its line and couldn't do it any more. What I mean is that it is not necessary to take that product out in every instance, but, as a matter of good operating practice, you must take it out or else you are not going to get the maximum efficiency out of your transportation [fol. 350] system. But that certainly is one of the factors that weighs very heavily upon it.

But I am saying this: Where you are assuming to price joint products, and assume for the moment there are joint products for this purpose, if you are attempting to price joint products on certain ratios, and it is recognized by all the authorities that those ratios can vary, as long as they sort of vary together, where you have one subject to wide fluctuation, and the other fairly steady, it is universally recognized that the method breaks down.

Now, in this case there was one piece of literature introduced in the record saying you can use some kind of averaging process, but over what period of time you are supposed to average, I don't know. That was the opinion of one writer upon the subject, but it seems to me it would be perfectly ridiculous to adopt a method of costing a product when you are doing the exact thing; today, you - making X dollars, tomorrow, XY dollars, and maybe the next day zero dollars. It just doesn't seem to be sensible.

Now, there is another factor we have to consider here, and tacitly it has been admitted by staff counsel that while the staff witness attempted to use, or purported to use a market value method, he did not use market value as to natural gas. Market value, he recognized to be the results of arm's length bargaining in a recent transaction, but the amount which he purported to use was a conglomerate mass of prices paid by Colorado Interstate Gas Company for gas, under contracts going back for 20 or more years, and by other companies in the field where he attempted to use this weighted average of the Texas Railroad Commission, and he admitted that so far as he knew there might

even be distress sales in that particular conglomerate mass. Now, that does not represent market value.

They say we pay a Texas production tax, 4.33 cents, I believe is the exact figure, but the Texas production tax is based upon statutory definition as to what you do with it, [fol. 351] and it is not market value. Market value again is recognized, and the witness himself recognized, is the price paid after arm's length bargaining in recent transactions.

I say by his own admission he has taken us away entirely from the market value method of allocation, and in effect has made no allocation whatsoever.

Now, in speaking of the method used by the company, staff counsel—and if I misquote him, I am sure he will correct me, I don't mean to do so—stated that the company used only $55,000 as the part of the joint costs applicable to gasoline extraction. We are talking about joint costs at this point, where they are still joint, before the point of split off where you have *in*dentifiable gasoline, and identifiable dry gas.

He fails to point out there are $93,000, in addition to the $55,000, of direct gasoline royalties, which are certainly charged, and charged by the study submitted by Colorado Interstate Gas Company, directly to the gasoline operations.

Now, one thing that struck me, he also sought support for using a five-cent value for natural gas because it is consistent with certain royalty payments, and for depletion purposes they used five cents, and then for the sake of consistency, we should use five cents for that purpose here. I am wondering why not, for the sake of consistency, we should not attribute five cents for rate making purposes also. That Panhandle gas comes out considerably less than five cents.

Commissioner Smith: You made no such claim in this case?

Mr. White: We did not, sir. I was just talking about consistency. I thought if the staff was going to be consistent up to one point they ought to carry it out the whole way.

Now, on the company method of costing these gasoline plant operations—I am sorry, I had intended to have a schematic drawing available for the Commission here, but [fol. 352] it did not develop. I have a few copies of an exhibit which was introduced in this case, if any of the Commissioners would care to see it, which is Exhibit 32, a schematic drawing of the Bivins gasoline plant.

A staff witness in this particular case did not attempt to make any study of the gasoline plant before he determined how he was going to cost the operations, he just used the application of the approach, or the relative market value method.

What I want to point out to the Commissioners is that this is a pretty complicated operation, at least it is complicated to me. Down in the lower left-hand corner, the wet gas which has not yet been stripped enters into the plant, passes through absorbers, where absorbing oil is brought in contact with it. This is a bank of three absorbers in this Bivins plant, in which case the clean oil absorbitive picks up the liquid fractions and carries it as enriched oil on over to another heading. Now, you will notice in the upper part of each one of these are dashed lines, we call joint gas and gasoline. This rich oil goes into reabsorbers which takes out still more, and is subject to various processes on down until again it is condensed or distilled, and finally you have a point of split off where this dashed line occurs.

Now, this represents the work of Mr. Otto Praeger, who is certainly a well qualified engineer. He has been dealing with this type of operation ever since he was discharged from the Army back in the early 20's. He went back in the Army during the course of the last war, and concerned himself with analogous problems. He is a man who redesigned this plant, and certainly is an expert to speak upon it.

It is his expert opinion, and he was able to be cross-examined at length upon it, and it was never shaken, that up to this split off point you have a joint operation. Now, the staff witness aside from a small amount of dehydration cost, never attributed one cent of cost to dry natural gas after the stream of wet gas entered the extraction

plant, although he recognized that it was necessary to take [fol. 353] out natural gasoline in order to make the gas transportable.

Mr. Spurrier, I think, admitted he had been inside a gasoline plant. He did not attempt, as was brought out on his cross-examination, to equate into his study any part of the actual business of operating the plant.

Mr. Praeger, on the other hand, as I have pointed out as to this Bivins plant—he is an expert engineer, on these things overall, redesigned the plant, knows intimately what is in it, and on the basis of his expert judgment he indicates that this is what the facts are.

Subsequent to exploring what goes on in the gasoline plant, and there was a similar drawing of the Fourway plant, Mr. Praeger split in detail, on the basis of actual studies, what happens in that plant, the application of labor to this, the application of material, the split up of investment between these various things.

After having that, our expert witness on allocation, Mr. James O'Connor, allocated these joint costs, and he did it on a volumetric basis, and by volumetric, I mean here that he did it for several reasons, one is that it is the Commission's practice usually to allocate cost on a volumetric basis, not referring to classification of cost, necessarily, but once you have costs classified, and decide how to spread them, you do it on a number of cubic feet, either taking it on the peak period, if it is demand cost, or on an overall basis.

He felt it was proper to use a volumetric basis for that reason, and also for the reason that gasoline and gas are themselves inseparable products, except what incidental amounts may come out through drips, and so forth, until you reach a point of separation, so consequently it is the overall volume which determines the size of field gathering lines, and so forth, and I think there are sound reasons for using this method.

[fol. 354] It is on that basis that he comes up with the percentage overall of 2 per cent for the Fritch gasoline operation, 1 per cent for the others, and it seems that if that is the result of a sensible method, that is the method

that should be used, so instead of having a $600,000 loss which the staff contends we have on this gasoline plant operation, we have shown a $600,000 profit under the facts of merger, where we give up 50 per cent of the Fourway and Bivins operation to the new hydrocarbon company, and where we give up 85 per cent of the net out of the Fritch gasoline plant operation.

Commissioner Draper: You are going to show that situation?

Mr. White: Our books will certainly show the situation. I don't know that there will be an allocation as we go along, but it will certainly show what money we make.

Commissioner Wimberly: There is a dispute as to the allocation.

Mr. White: Exactly. There is no fundamental dispute on the other. There is some variation between the two, but when you come down to the real nub of this problem, that isn't what matters, it is the method you use to allocate these costs.

Now, on depreciation, it is sought to reduce the company's claim by approximately $141,000, and I want to point out that the depreciation method used in the presentation of its case here by the company is the method reflected on the company's books, and that is the remaining life method of 25 years from January 1, 1948.

It may be that we are not claiming enough depreciation, because the Commission itself, 25 years from that date brings us out to December 31, 1972, and since this problem is tied into reserves, and the staff counsel himself has recognized it is so tied in, I would like to quote just one particularly appropriate part of the Commission's Opinion 209, which was issued in the merger case. There they were talking about the availability of gas in the future, the [fol. 355] the Commission was, and is response to the contentions made by the staff there would be available Canadian acreage in the future to the ratepayers. It says the figure advanced is based upon the assumption that gas will be available from the Canadian acreage from Colorado's Clayton-Denver line after 1972. We think that this assumption is unfounded, since the record shows the pro-

duction from the Canadian acreage will probably have declined by 1972 to such a point that the volume of gas available therefrom will be sufficient only to supply the requirements of the Texas markets which retain their priority over those in the Rocky Mountain area.

Now, if depreciation policy is tied into the present reserves of the company, and this is what the Commission has to say about our present run-out period of 1972, it may well be that we should be claiming more.

In addition to that, the Commission has limited us in Docket G-1677, under a provision which presently is subject to rehearing, I recognize that, because the Commission has so acted, but it is because of the general present reserve situation of the company.

Now, the facilities that are involved here are tied into those reserves, and if there is some misgiving about our ability to produce gas for our main transmission system, even up to 1972, I submit the remaining life method, which we are using at present, to run out in 1972 is completely realistic, if perhaps not a little too much on the conservative side from the standpoint of the all annual accrual.

The Chairman: Are you going to be consistent and claim that lesser depreciation, then, that is the time for depreciation, and discard the five-cent depletion?

Mr. White: I am sorry.

The Chairman: Are you going to deny the one and accept the other, just to be consistent?

Mr. White: I am not denying the depreciation. All I am asking is that we take it per books. Our taxes, as a matter of fact, on our books, if that is what the Chairman [fol. 356] means, are being accrued at 3.17.

The Chairman: If you want to depreciate on a lesser period of time than the 1972 period, that is what you are seeking——

Mr. White: I am not seeking to do that. What I am pointing out here is perhaps what we are doing is not enough. We are not changing it. We are continuing the remaining life method, which would run us out in December 1972.

The Chairman: You are seeking a higher rate?

Mr. White: We are not seeking a higher rate than we are booking. We are saying we are entitled to a higher rate than the staff says we are entitled to.

Commissioner Smith: And is the difference simply between straight line and remaining life?

Mr. White: No, there is a service life of 25 years from 1952 used on new facilities, which would run those new facilities out in 1977. But, at the same time, the reserves would not last that long, except perhaps on some diminishing balance basis, if that might be the policy of the Commission, where you are not going to utilize facilities in the future after the expiration of the remaining life, or even a straight line period, as far as that is concerned, Commissioner Smith.

Now, on certain miscellaneous expenses—do I have 12 minutes, Mr. Chairman?

The Chairman: Yes, you have.

Mr. Smith: On the miscellaneous expenses, the subject has been thoroughly briefed by Colorado Interstate. Since we are here fixing rates for the future, I think it is the admonition of most authorities that regulatory commissions should allow what is necessary for the company to keep in business, and to maintain its usual methods of doing business, keep progress——

[fol. 357] Commissioner Draper: To what end?

Mr. White: I don't think for one moment that it helps the public to have a company that isn't going to be assured a return and expenses which it is expected it would meet.

Now, on regulatory commission expenses, I am going to skip over these except the one which has caused so much pain. On regulatory commission expenses, the fee of Mr. Houlihan, which the Commission staff sought to eliminate, they say is non-recurring, related to gasoline plant costing. I think this case is the best example that that is not a non-recurring item. It is a question that is apt to come up before this Commission very often. While Mr. Houlihan testified on that subject in the merger case, and the merger won't be reoccurring, certainly the question of costing joint products in these gasoline plant operations will recur in the future.

The regulatory commission expense relates, as Mr. Goldberg said, to review of these rate proceedings. We have cited cases, the opinion of Mr. Justice Cordoza, in which he recognizes that is a legitimate item of expense.

They have also sought to amortize it over five years, what they do allow over five years rather than three years. They do that on the basis that that is the Commission's policy. I state with its great influx of regulatory cases, this Commission is certainly conscious of how that has increased in the last several years, it is time that this period be shortened, because you are going to have running concurrently too doggone many amortization periods of regulatory commission expenses.

On salaries and wages, this additional estimated increase —and it has been the company's policy to grant increases, as the record shows, based on cost of living, and promotional increases, and so forth—we think are wholly justified by the record, and that has been analyzed in the briefs of Colorado Interstate Gas Company.

On the amount of gas royalties, I don't recall too much said by staff counsel, but there has been an adjustment of [fol. 358] gas royalties based upon the settlement of an actual claim, and on the settlement of lawsuits, and we are attempting to get rid of all of those drainage suits, is what they are. They came up in the Panhandle field. They have been brought by the royalty owners of the former Canadian River Gas Company, and that was a matter of considerable concern during the progress of the merger, as the record in that case will indicate, so much so that it was a matter of specific question by staff counsel in that case to me as counsel for Colorado Interstate as to whether the merger would mean it would cost more on drainage cases if a merger took place than if it hadn't taken place, and I said no it wouldn't, but they have got to get rid of these drainage cases and keep our royalty owners satisfied on the basis of what happens in the future.

Now, there is involved the compensation to directors of the company, $5000, each, a year, and also the fees to be paid to the Chairman and other non-employee members of the executive committee.

I would like to point out that Exhibit 43 points out that Mr. Spencer, who was one of these selling stockholders, one of the lame ducks, so to speak, stated that he was not going to take his $15,000, and he didn't take his $5000. The amount is still payable to the other non-employee member of the executive committee. Whether he has been elected yet or not, I frankly don't know. I have been busy on other things, and there have been directors meetings within the past two weeks, and I am not sure whether the vacancy has been filled or not. But it will be filled.

The question centers around this fact: Should the ratepayer have to pay for that? That is the subject of the inquiry, as I see it. Now, the executive committee is a recognized adjunct of corporate management, and I don't think it is up to a regulatory commission until facts show it is an unreasonable expenditure, to override the discretion of management in deciding that this should be done.

[fol. 359] Now, this company is in effect a new company. It is actively seeking gas reserves, it has to have them, this Commission has stated it has to have them, and you can't do that sort of thing without paying for somebody who is willing to scout around and send people out and do whatever is necessary to get those reserves for the company. It seems to me——

The Chairman: Is that what the executive committee or directors are going to do, scout around for reserves?

Mr. White: They are already engaged in doing it, Mr. Commissioner.

Commissioner Smith: You mean they are authorizing it to be done?

Mr. White: And they, themselves, are doing a considerable amount of work on it.

Commissioner Smith: Can you enlighten me on this, perhaps this isn't a proper question, I don't know, about this so-called lame duck action, as to who was present, and what the voting was?

Mr. White: I don't know who was present, but I understand one director dissented, Mr. Parks, and he is a director. Public Service of Colorado owns only 15 per cent of the stock in that matter.

Commissioner Smith: And being a principal customer of the company.

Mr. White: And being a principal customer of the company. Whether that is what motivated him or not, I don't know.

Commissioner Smith: I think it would be very helpful for us to have that record here.

Mr. White: I think the implication was left in the record that the request was made for these minutes. I am sure it was not made. It wasn't made while I was conducting the hearings, and Mr. McGee was conducting them when I wasn't.

[fol. 360] The Chairman: Well, the record will speak for itself in that respect.

Mr. White: Of course it will.

Commissioner Wimberly: How many directors are there of Colorado Interstate?

Mr. White: Seven.

Commissioner Wimberly: What fees had they been getting prior to this action?

Mr. White: $100 a meeting, or $150 a meeting, I believe.

Commissioner Smith: Would you have any objection, Mr. White, to supplying that minute of this particular meeting, if the Commission should decide to reopen this record and request it?

Mr. White: I have no objection, sir.

Commissioner Smith: Can you speak for the company?

Mr. White: I think I can speak for the others. I have no objection to doing it, and if the Commission deems it advisable to inquire into it, from that standpoint I am personally willing, and will so recommend to the others.

That covers the miscellaneous general expenses. The employee's welfare and pension expenses I am going to have to submit on the brief, because I have one further word to say, and I do ask the Commission carefully to review the untouched questions as well as the others.

That is the end result of what is proposed here. We are used to talking in terms of end results these days, particularly since the Hope case in the Supreme Court of the United States. It was rather surprising to me, on getting the reply brief from the staff in this case in which they

have their Table 2 as an appendix to the brief, to show that for total jurisdictional sales on the Denver system, in the Rocky Mountain area, excluding Natural Gas Pipe Line of America, the total average cost of the gas is 11.46 cents a thousand. This is after the gas has been produced, after it has been compressed, after it has been stripped, after it [fol. 361] has been transported, 350 miles in one case, 320 miles in another. The average cost, city gate price, 11.46 cents.

Now, this company—and it is in the record in this case—in its acquisition recently of gas supplies, has been paying roughly 10 cents a thousand at the wellhead. After that, the gas has to be transported at least 310 miles, and usually more because it also has to be gathered. Now, we are interested here in the overall reasonableness of this company's present rates. We aren't proposing a rate increase, this is a 5(a) case. Somebody is contending these rates of ours are unreasonable.

It seems to me that that in itself is one of the most telling things that you could cite, a company today being exhorted to get more gas reserves, and having to pay a price at the wellhead which is practically the same as the price shown at the city gate in the Rocky Mountain area in this case.

I think, Mr. Chairman, I will give you back the remaining minute.

Thank you very much, sir.

The Chairman: Mr. Goldberg?

You have about 17 minutes, I believe.

Rebuttal Argument of Jacob Goldberg

Mr. Goldberg: In reference to the $4,000,000-figure Mr. White gave as to the difference between the cost of service allocated between the Staff and the company, I should like to observe that about half of that is made up of the taxes that result because of the difference in the cost of service in the beginning, and which of course merely means that they have got to make so much more revenue to pay for the taxes associated.

Actually, if you take the taxes away, there is only about a $2,000,000 difference.

[fol. 362] Now, Mr. White mentioned something about the Staff Exhibit 25 items, eliminating 6, and then there were another 18 we included. The 6 or 7 we eliminated on the rate of return study of Mr. Goubleman were financed before 1946. The table was made up from 1935 to date. Five or six had financed prior to 1946. Obviously the economic situation as to natural gas companies has changed radically since the termination of World War II, so he eliminated those.

Now, I don't understand the business of eliminating the Tennessee Gas Transmission stock issue. To me that is a natural gas company like any other natural gas company, and to try to anticipate what investors do about that stock as contrasted with what investors do about another stock is just hopeless. Every stock has a certain discount —there are certain aspects as to every stock as to what investors regard, and to arbitrarily say a whole issue of Tennessee Gas should be eliminated because of what Mr. Merrill says the investor is paying more for future earnings just doesn't make sense. They discount everything. They discount low earnings, they discount increased earnings, they discount the fact that the president is an old man, is aggressive, or whatever it is. Every stock has a discount factor, and to arbitrarily eliminate some issues just to come up with the issues you want just doesn't seem fair to me, and we took in everything, Tennessee, Texas Eastern, Texas Gas, all of them, because they are all gas companies, and they are all discounted for some reason or other.

Now, on this business of the depletion allowance for tax purposes, five cents against the 3.17, Mr. Commissioner Smith, I forgot to answer to your question about making a statement at one time, and changing it at another time, for important is this on the theory of estoppel. When you make a statement and get something, if you want to recast your statement or deny your statement, the least you ought to do with good conscience is give back what you took, and nobody yet has mentioned the fact for all this time in 1952 it is estimated the West-Pan Hydro Carbon [fol. 363] Company is going to get better than $1,400,000. That, Mr. White doesn't say, while they are claiming the

3.17 rate we are going to give back $1,400,000. No, they want to give up the $1,400,000, which would have been a credit to the cost of gas, but they say we may be harmed if we don't get the 3.17 rate. As a matter of fact, they are claiming more than the 3.17 rate, and they were claiming more than that at the time of the merger proceedings. I can't see how there is much merit in Mr. White's statement about the 3.17 rate.

Now, so far as costing the joint operations, Mr. White's statement reminded me of the oft-quoted Justice Brandeis, "It is must easier to criticize a formula than to derive one."

That is the situation here. There is no formula that is perfect. It is a joint operation, it is a question of judgment, and as a practical business outlook are you going to say that $55,000 out of better than $4,500,000 is a proper cost, or are you going to say that roughly 20 per cent is a proper cost? We maintain something under 20 per cent is the proper cost when you come to allocate the joint cost, and so far as the gasoline plant is concerned, while the chart is very interesting, and shows how a gasoline plant operates, the chart shows that the gasoline plant is for the gasoline operation, and if it is for the gasoline operations, it is the gasoline that *that* has to stand the expense.

Now, so far as the depreciation, and the company ending business in 1972, Mr. White has cleverly incorporated the opinion of the Commission pertaining to the Panhandle reserves as if it applies to all the reserves of Colorado Interstate. That isn't so. Our witnesses, when they estimated the 25-year service life of the new facilities, said not only are the Panhandle reserves assumed, if you want, to expire in 1972, but the Hugoton reserves are expected to continue to 1976, and also the Keyes Field, you are just attaching a new field, and he said there is more exploration going on. Mr. White said the executive committee is also hunting for new gas. Well, we take that into consideration in fixing the service life, so we maintain when you look at the whole thing, and just don't try to read in what the [fol. 364] Commission said about the Panhandle Field as illustrative of what happens to all the reserves of the

company, you will come up with what the Staff said was the correct service life.

So far as Mr. Houlihan's testimony in the merger proceedings, testifying to an allocation for the gasoline operations, the short answer to that is this: We have allowed in this hearing all the rate case expenses that they have estimated before the Commission, including the testimony of Mr. Praeger, the testimony of Mr. O'Connor, all the people who testified on allocation, they have been paid. Houlihan was paid in the other case, and that is the end of it. I can't see why Mr. Houlihan's salary should be put back here in this proceeding.

In conclusion I should like to note that Mr. White read off the figure of the excess revenues based on the 6 per cent return. If you will look at Table 1 of the reply brief, the excess revenues based on the 5¾ per cent return is $3,554,250 of jurisdictional business.

Thank you.

The Chairman: We will take the matter under advisement.

Whereupon, at 12:05 p. m., the oral argument in the above-entitled matter was concluded.

[fol. 365-366]

EXHIBIT 1

A. E. WISKUP

SCHEDULE 3

Docket No. G-1115

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Statement Reflecting the Staff's Computation of Federal Income Tax Giving Effect to the Merger
For the Year Ended June 30, 1951

	Reference	Total	Eliminations for Tax Computation Purposes	Total for Tax Computation Purposes
Return at 6%	Sch. 1	$2,560,816.42	$ —	$2,560,816.42
Add: Other Income				
Revenue from Lease of Other Physical Property	Sch. 7	31.20	—	31.20
Interest Revenues	Sch. 7	284.03	—	284.03
Miscellaneous Nonoperating Revenues	Sch. 7	669.33	—	669.33
Nonoperating Revenue Deductions	Sch. 7	(1,336.63)	—	(1,336.63)
Total Other Income		(352.07)	—	(352.07)
Less: Income Deductions				
Interest on Long-Term Debt	Sch. 7	568,333.32	(432.21)	567,901.11
Interest Charged to Acct. 142.2—Other Preliminary Survey and Investigation Charges		60,000.00	—	60,000.00
Amortization of Debt Discount and Expense	Sch. 7	3,488.25	—	3,488.25
Amortization of Premium on Debt—Cr.	Sch. 7	(999.96)	—	(999.96)
Other Interest Charges	Sch. 7	79.36	—	79.36
Interest Charged Construction—Cr.	Sch. 7	(30,432.21)	30,432.21	—
Miscellaneous Income Deductions				
Staff Adjustments	Sch. 7	78,686.69	(78,686.69)	—
Other—Contributions, etc.	Sch. 7	13,385.84	129.11	13,514.95
Total Income Deductions		692,541.29	(48,557.58)	643,983.71
Add: Depreciation and Depletion for Rate Case Purposes	Sch. 1	1,831,495.57	—	1,831,495.57

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SCHEDULE 3

Docket No. G-1115

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Statement Reflecting the Staff's Computation of Federal Income Tax Giving Effect to the Merger
For the Year Ended June 30, 1951

	Reference	Total	Eliminations for Tax Computation Purposes	Total for Tax Computation Purposes
Less: Tax Return Deductions				
Depreciation for Tax Purposes—Colorado Interstate Gas Company Properties	Sch. 3a	1,329,622.18	—	1,329,622.18
Depreciation for Tax Purposes—Canadian River Gas Company Properties	Sch. 3b	355,329.13	—	355,329.13
Depletion for Tax Purposes	Sch. 3c	931,027.13	—	931,027.13
Intangible Productive Well Drilling Costs		1,056,049.48	—	1,056,049.48
Property Removal Costs		22,775.63	—	22,775.63
Total Tax Return Deductions		3,694,803.55	—	3,694,803.55
Net Taxable Income After Tax		$ 4,615.08	($48,557.58)	53,172.66
Less: Credit for Dividends Paid on Preferred Stock (30% x $120,000)				36,000.00
Tax Base				$ 17,172.66
Normal Tax at 25% (25/75)				$ 5,724.22

Note: No surtax to be computed as surtax applies to income over $25,000.

(Here follows Schedule 8, folios 367-382)

[fol. 367–382]

Docket No. C–1115

A. E. WISKUP

SCHEDULE 8

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Balance Sheets Giving Effect to the Merger
as at June 30, 1950 and 1951

Assets and Other Debits	As of June 30, 1950	As of June 30, 1951
Utility Plant		
Gas Plant in Service	$53,973,577.25	$56,780,715.30
Construction Work in Progress	950,359.18	1,317,289.00
Gas Plant Held for Future Use	46,648.30	46,648.30
Total Utility Plant	54,970,584.73	58,144,652.60
Investment and Fund Accounts		
Other Physical Property	13,219.07	2,011.55
Current and Accrued Assets		
Cash	2,217,709.13	3,702,029.92
Special Deposits	610,483.37	6,083.28
Working Funds	75.00	75.00
Notes Receivable	914.77	452.25
Accounts Receivable	1,097,265.51	1,285,318.83
Materials and Supplies	1,657,714.51	1,320,459.81
Prepayments	62,116.64	57,511.71
Total Current and Accrued Assets	5,646,278.93	6,371,930.80
Deferred Debits	58,337.00	179,896.19
Total Assets and Other Debits	$60,688,419.73	$64,698,491.14

Liabilities and Other Credits	As of June 30, 1950	As of June 30, 1951
Capital Stock		
Common	$ 2,352,942.17	$ 2,352,942.17
Preferred	2,000,000.00	2,000,000.00
Total Capital Stock	4,352,942.17	4,352,942.17
Long-Term Debt	19,600,000.00	18,800,000.00
Current and Accrued Liabilities		
Accounts Payable	1,075,353.58	1,217,590.85
Taxes Accrued	2,731,838.73	3,883,456.35
Interest Accrued	111,666.69	109,000.01
Other Current and Accrued Liabilities	9,513.18	99,136.45
Total Current and Accrued Liabilities	3,928,372.18	5,309,183.66
Deferred Credits	18,749.25	17,749.29
Reserves for Depreciation and Depletion	13,893,950.12	15,747,865.70
Employees Death Benefit Reserve	—	3,500.00
Contributions in Aid of Construction	137,342.27	139,302.44
Earned Surplus	18,757,063.74	20,327,947.88
Total Liabilities and Other Credits	$60,688,419.73	$64,698,491.14

Note: Above represent balance sheets per books combined with intercompany receivables and payables eliminated.

[fol. 383–384]

Page 12

EXHIBIT 11

Natural Gas Common Stocks Offered to the Public During the Period 1935 to Date
With Earnings-Offering Price Ratio and Cost of Financing

Line No.	Name of Issue	Approximate Offering Date	No. of Shares Offered	Price to Public		Price Per Share to Underwriter	Line No.
				Total	Per Share		
	(a)	(b)	(c)	(d)	(e)	(f)	
1	Kansas Pipe Line & Gas Co., (1), $5.00 Par (16)	Aug. 1936	110,000	$ 550,000	$ 5.00	$ 4.82	1
2	Northern Natural Gas Co., $20.00 Par (6)	Sept. 1941	355,250	11,368,000	32.00	29.65	2
3	Kansas-Nebraska Natural Gas Co., Inc., $5.00 Par (16)	Dec. 1941	48,468	315,042	6.50	5.49	3
4	Kansas-Nebraska Natural Gas Co., Inc., $5.00 Par (16)	May 1944	17,765 (9)	124,355	7.00	6.22 (9)	4
5	Montana-Dakota Utilities Co., $5.00 Par (16)	Oct. 1945	223,352	2,568,544	11.50	10.55	5
6	Tennessee Gas Transmission Co., $5.00 Par (4)	Jan. 1946	812,100 (4)	9,745,200	12.00	11.10	6
7	Tennessee Gas Transmission Co., $5.00 Par (5)	Apr. 1946	484,444 (5)	9,567,769	19.75	18.65	7
8	El Paso Natural Gas Co., $3.00 Par (16)	July 1946	2,697 (12)	113,274	42.00	41.62	8
9	Texas Eastern Transmission Corp. No Par (13)	Nov. 1947	3,550,000 (13)	33,725,000	9.50	8.50	9
10	Northern Natural Gas Co., $10 Par (14)	Dec. 1947	710,500 (14)	19,183,500	27.00	25.80	10
11	Washington Gas Light Co., No Par (17)	Jan. 1948	13,790 (17)	279,248	20.25	19.25	11
12	Montana-Dakota Utilities Co., $5.00 Par (15)	June 1948	150,000	1,875,000	12.50	11.60	12
13	Tennessee Gas Transmission Co., $5.00 Par (19)	Sept. 1948	400,000	12,100,000	30.25	28.60	13
14	Mississippi River Fuel Corp. $10 Par (18)	Jan. 1949	144,200 (18)	4,326,000	30.00	28.00	14
15	Mississippi River Fuel Corp., $10 Par (20)	Apr. 1949	435,282 (20)	13,058,460	30.00	(20)	15
16	Texas Gas Transmission Corp., $5 Par (21)	Aug. 1949	218,625	2,623,500	12.00	11.10	16
17	Tennessee Gas Transmission Co., $5 Par (22)	Sept. 1949	400,000	12,100,000	30.25	28.80	17
18	Equitable Gas Co., $8.50 Par (23)	Mar. 1950	2,000,000	48,500,000	24.25	22.88	18
19	Texas Gas Transmission Corp., $5 Par (24)	Mar. 1950	193,306	3,527,835	18.25	17.13	19
20	Tennessee Gas Transmission Co., $5 Par (2)	Oct. 1950	250,000	7,500,000	30.00	28.55	20
21	Washington Gas Light Company, No Par (25)	Apr. 1951	20,596	507,279	24.63	(3)	21
22	Tennessee Gas Transmission Co., $5 Par (26)	Apr. 1951	400,000	9,600,000	24.00	22.75	22
23	Midsouth Gas Company, $1.00 Par (27)	July 1951	100,000	675,000	6.75	(3)	23

[fols. 385-386]

Natural Gas Common Stocks Offered to the Public During the Period 1935 to Date
With Earnings—Offering Price Ratio and Cost of Financing

Line No.	Net Proceeds Per Share to Company	Expenses to Issuing Co. Incidental To Flotation	Cost of Flotation per share		Earnings per Share		Earnings—Offering Price Ratio	Line No.
			Amount	Percent of Price to Public				
	(g)	(h)	(e−g) (i)	(i÷e) (j)	12 Mos. Ended (k)	Amount (l)	(m)	
1	$4.73	$0.09	$0.27	5.4%	Mar. 31, 1937	$0.71 (8)	14.2%	1
2	(3)	(3)	(3)	(3)	Dec. 31, 1940	3.65 (6)	11.4	2
3	5.41	0.08	1.09	16.8	Nov. 30, 1941	0.54 (11)	8.3	3
4	6.15 (9)	0.07 (9)	0.85 (9)	12.1 (9)	Dec. 31, 1943	0.82 (10)	11.7	4
5	10.47	0.08	1.03	8.9	Dec. 31, 1944	0.60 (7)	5.2	5
6	11.01	0.09	0.99	8.3	Nov. 30, 1945	2.07 (4)	17.3	6
7	18.62	0.03	1.13	5.7	Dec. 31, 1945	2.46 (5)	12.5	7
8	41.11	0.52	0.89	2.1	May 31, 1946	3.39 (12)	8.1	8
9	8.45	0.05	1.05	11.1	(13)	(13)	(13)	9
10	25.70	0.10	1.30	4.8	Sept. 30, 1947	3.43 (14)	12.7	10
11	18.71	0.54	1.54	7.1	Nov. 30, 1947	1.45 (17)	7.1	11
12	11.44	0.16	1.06	8.5	Dec. 31, 1947	1.39 (15)	11.1	12
13	28.41	0.19	1.84	6.4	Dec. 31, 1947	2.40 (19)	7.9	13
14	27.51	0.49	2.49	8.3	Dec. 31, 1947	2.46 (18)	8.3	14
15	(20)	(20)	(20)	(20)	Dec. 31, 1948	3.49	11.6	15
16	10.92	0.18	1.08	9.0	May 31, 1949	0.75	6.3	16
17	28.68	0.12	1.57	5.2	July 31, 1949	2.24	7.4	17
18	22.83	0.05	1.42	5.9	Dec. 31, 1949	1.84	7.6	18
19	16.72	0.41	1.53	8.4	Dec. 31, 1949	0.81	4.4	19
20	28.31	0.24	1.69	5.6	Aug. 31, 1950	1.84	6.1	20
21	(3)	(3)	(3)	(3)	Dec. 31, 1950	2.84	11.5	21
22	22.64	0.11	1.36	5.7	Dec. 31, 1950	1.73	7.2	22
23	(3)	(3)	(3)	(3)	Dec. 31, 1950	0.47	7.0	23

[fols. 387-388]

EXHIBIT 11
Page 13

Earnings—Price Ratios of Outstanding Common Stocks of Seven Natural Gas Companies
January 1940 To Date

	1940	1941	1942	1943	1944	1945	1946	1947	1948	1949	1950	1951	1952
Jan.	10.5%	11.8%	13.7%	12.4%	10.4%	9.4%	6.6%	7.6%	9.4%	8.9%	6.8%	7.4%	
Feb.	9.8	12.3	13.3	11.8	10.3	9.1	7.2	7.8	9.9	9.2	6.8	7.3	
Mar.	10.0	12.4	15.0	11.6	10.6	9.4	6.8	8.3	9.2	8.8	6.7	7.3	
Apr.	10.2	13.6	16.1	11.3	10.9	9.1	6.7	8.4	8.7	9.1	6.9	7.4	
May	12.9	13.1	16.2	10.5	10.8	9.3	6.8	9.2	8.5	9.1	6.7	7.6	
June	11.3	12.7	16.3	10.6	10.8	8.5	6.9	9.1	8.4	9.3	7.2	7.6	
July	13.3	11.5	15.7	10.3	10.7	8.9	7.1	8.9	8.5	9.1	8.5	6.7	
Aug.	13.3	11.5	15.1	10.3	10.3	8.8	7.6	9.4	8.4	8.5	8.0	6.6	
Sept.	13.0	11.5	14.8	10.1	10.4	8.7	8.1	9.2	8.7	8.3	7.7		
Oct.	12.3	11.9	14.6	10.1	10.0	8.2	8.0	8.9	8.6	7.6	7.9		
Nov.	11.9	14.2	13.8	10.6	10.3	7.5	8.1	9.0	9.8	7.3	8.0		
Dec.	11.9	15.6	13.5	10.6	10.0	7.4	7.9	9.0	9.3	6.8	7.9		
Straight Average	11.7%	12.7%	14.8%	10.9%	10.5%	8.7%	7.3%	8.7%	9.0%	8.5%	7.4%		

Note: The above data are based on the closing market quotations at the end of the month and the latest available earnings for a twelve months period immediately preceding the particular month. Also, the earnings-price ratios are based on weighted figures.

Source of Data: Moody's Public Utility Cumulative Index, Standard & Poor's Stock Guide and Bank and Quotation Record.

[fols. 389-392]

EXHIBIT 11
Page 13a

Earnings-Price Ratios and Yields on 7 Natural Gas Pipe Line Company Common Stocks
July 31, 1951

Company	No. Shares Out-standing (000)	Market Price		Earnings			E.P.R.	Div. Rate	Yield
		7/31/51	Total (000)	12 Mos. Ended	Per Share	Total (000)			
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
Consolidated Gas Utilities Corp.	886	$11.63	$10,304	4/30/51	$1.52	$1,347	13.1	$0.75	6.4%
El Paso Natural Gas Company	2,701	29.88	80,706	5/31/51	2.88	7,779	9.6	1.60	5.4
Lone Star Gas Company	5,499	27.63	151,937	6/30/51	1.89	10,393	6.8	1.40	5.1
Mountain Fuel Supply Company	1,990	17.00	33,830	12/31/50	0.99	1,970	5.8	0.60	3.5
Northern Natural Gas Company	2,741	38.00	104,158	3/31/51	2.09	5,729	5.5	1.80	4.7
Panhandle Eastern Pipe Line Co.	3,240	54.50	176,580	3/31/51	2.73	8,845	5.0	2.00	3.7
Southern Natural Gas Co.	1,711	45.38	77,645	3/31/51	3.63	6,211	8.0	2.50	5.5
Totals			$635,160			$42,274	6.7%		

Source of Data: Standard & Poor's Stock Guide, August, 1951.

[fols. 393-404]

EXHIBIT 13

Docket No. G-1115

SCHEDULE B

Sheet 1 of 3

Colorado Interstate Gas Company
Canadian River Gas Company

Return at Assumed Rate of 6%
Based on Estimates of Colorado Interstate Gas Company
In Application In Docket G-1677, as Adjusted Years 1951, 1952 and 1953

	Source	1951	1952	1953
Colorado Interstate Gas Co.	Sch. B, Sheet 2	$2,050,022	$2,246,679	$2,213,738
Canadian River Gas Co.	Sch. B, Sheet 3	999,875	1,299,020	1,367,339
Total		$3,049,897	$3,545,699	$3,581,077

[fols. 405–410]

EXHIBIT 18

Docket No. G–1115

Colorado Interstate Gas Company

Allocation—Excess Earnings

Particulars	Excess Earnings Based on Company Estimates in Docket No. G–1677 As Adjusted			Line
	1951	1952	1953	
Sales to Other Utilities				
Production System—Firm				
Amarillo Oil Co.	$ (106,000)	$ (127,453)	$ (77,834)	1
Transmission System—Firm				
P–1	162,841	195,798	119,572	2
G–1	1,508,967	1,814,360	1,108,010	3
Clayton Gas Co.	1,728	2,078	1,269	4
Dalhart Gas Co.	2,304	2,770	1,692	5
Total Firm	1,675,840	2,015,006	1,230,543	6
Transmission System—Interruptible				
I–1	47,815	57,492	35,110	7
I–2	91,598	110,136	67,259	8
Clayton Gas Co. (Ind.)	(576)	(693)	(423)	9
Dalhart Gas Co. (Ind.)	(1,920)	(2,309)	(1,410)	10
Total Interruptible	136,917	164,626	100,536	11
Total Transmission System	1,812,757	2,179,632	1,331,079	12
Leased Transmission System				
Nat. Gas P.L. Co. of America	(159,384)	(191,641)	(117,033)	13
Total Sales to Other Utilities	$1,547,373	$1,860,538	$1,136,212	14
Direct Sales				
Production System				
Firm	$ 12,482	$ 15,008	$ 9,165	15
Interruptible	768	924	564	16
Total Production System	13,250	15,932	9,729	17
Transmission System				
Firm	9,025	10,852	6,627	18
Interruptible	350,646	421,611	257,474	19
Total Transmission System	$ 359,671	$ 432,463	$ 264,101	20
Total Direct Sales	$ 372,921	$ 448,395	$ 273,830	21
Total System Sales	$1,920,294	$2,308,933	$1,410,042	22
Total Jurisdictional	$1,652,989	$1,987,530	$1,213,761	23

Note: Jurisdictional Sales = Line 14—Line 1—Line 5—Line 10

( ) Indicates Red Figures

[fols. 411–416]

EXHIBIT 21

Schedule No. 1

Canadian River Gas Company
Colorado Interstate Gas Company

Estimated Cost of Service and Excess Revenues
Year 1952

Line No.		Reference (1)	Total (2)
1	Gas Service Revenues	Sch. 3	$17,962,532
2	Cost of Service		
3	Operating Revenue Deductions		
4	Gasoline Net Revenues	Sch. 5	(598,218)
5	Other Gas Revenues—Rent	Sch. 4	(37,500)
6	Production Expenses		
7	Gas Purchased	Sch. 6	2,082,000
8	Gas Used in Operations	Sch. 6	(270,300)
9	Other Production Expenses	Sch. 7	1,907,669
10	Transmission Expenses		
11	Operation & Maintenance	Sch. 7	2,385,700
12	Rental of Leased Facilities	Sch. 7	443,000
13	Distribution Expenses	Sch. 7	163,166
14	Administrative & General	Sch. 7	1,255,126
15	Sub-Total		7,330,643
16	Depreciation	Sch. 8	2,678,673
17	Depletion	Sch 9	57,688
18	Taxes—Federal Income	Sch. 10	2,245,479
19	—State Income	Sch. 11	63,765
20	—Other	Sch. 12	1,835,229
21	Total Operating Rev. Ded.		14,211,477
22	Return at 6.5%	Exh. 20	3,704,545
23	Total Cost of Service		$17,916,022
24	Excess Revenues		$ 46,510

(Here follows Exhibit 26 folios 417-424)

[fols. 417–424]

EXHIBIT 26

SCHEDULE A-1

Docket No. G-1115

Colorado Interstate Gas Company (Merged)
Estimated Excess Revenues and Cost of Service
Based on Estimates of Colorado Interstate Gas Company in Docket G-1115
As Adjusted
Year 1952

Line No.	(1)	Per Schedule No. 1 of Exhibit 21 (2)	Staff Reclassifications Per Schedule A-2 Reference (3)	Staff Reclassifications Per Schedule A-2 Amount (4)	As Reclassified (5)	Staff Adjustments Reference (6)	Staff Adjustments Amount (7)	As Adjusted (8)
1	Gas Service Revenues	$17,962,532			$17,962,532			$17,962,532
	Cost of Service							
2	Gas Purchased	$ 2,082,000	Entry No. 1	($2,082,000)	$ —	—	$ —	$ —
3	Operating Expenses	—	Entry No. 1	7,966,361)	—	—	—	—
			Entry No. 2	505,802)	8,472,163	Sch. A-3	(54,456)	8,417,707
4	Depreciation	2,678,673	—	—	2,678,673	Sch. A-4	(140,934)	2,537,739
5	Depletion	57,688	—	—	57,688	—	—	57,688
	Taxes:							
6	Federal Income	2,245,479	—	—	2,245,479	Sch. A-5	(2,118,252)	127,227
7	State Income	63,765	—	—	63,765	Sch. A-5	(59,948)	3,817
8	Other	1,835,229	—	—	1,835,229	—	—	1,835,229
9	Return	3,704,545	—	—	3,704,545	Sch. A-7	(274,666)	3,429,879
10	Other Gas Revenues	(37,500)	—	—	(37,500)	—	—	(37,500)
11	Gasoline Revenues	—	Entry No. 2	(1,104,020)	(1,104,020)	—	—	(1,104,020)
12	Loss on Gasoline Operations Not Chargeable to Ratepayers	—	—	—	—	Sch. A-8	(601,260)	(601,260)
13	Gasoline Net Revenues	(598,218)	Entry No. 2	598,218	—	—	—	—
14	Gas Used in Operations	(270,300)	Entry No. 1	270,300	—	—	—	—
15	Other Production Expenses	1,907,669	Entry No. 1	(1,907,669)	—	—	—	—
16	Transmission Expenses—Operation and Maintenance	2,385,700	Entry No. 1	(2,385,700)	—	—	—	—
17	Transmission Expenses—Rental of Leased Facilities	443,000	Entry No. 1	(443,000)	—	—	—	—
18	Distribution Expenses	163,166	Entry No. 1	(163,166)	—	—	—	—
19	Administrative and General	1,255,126	Entry No. 1	(1,255,126)	—	—	—	—
20	Total Cost of Service	$17,916,622		$ —	$17,916,022		($3,249,516)	$14,666,506
21	Excess Revenues	$ 46,510			$ 46,510			$ 3,296,026

( ) Denote red figures.

[fols. 425–436]

EXHIBIT 26

SCHEDULE A–7

Docket No. G–1115

Colorado Interstate Gas Company (Merged)

Staff Adjustment of Return
Year 1952

		Adjustment of Return
Decrease in return due to substitution of a 6% rate for the 6½% rate:		
Return, per Sch. 1 of Exh. 20 (Rate base of $56,993,006 times 6½%)	$3,704,545	
Above return using a 6% rate ($56,993,006 times 6%)	3,419,580	$ 284,965
Decrease in return due to staff adjustment of Regulatory Commission Expense (Per Sch. A–3):		
Adjustment of $54,456 times 1/8 equals $6,807 working capital times 6%		408
Total Decreases		285,373
Increase in return due to staff adjustment of depreciation provision:		
Decrease of $140,934 in provision (Per Sch. A–4) is reflected in the reserve for depreciation ending balance on Sch. A–19, divided by 2 the decrease gives $70,467 less average reserve for depreciation and higher rate base in Sch. A–15 than in Sch. 1 of Exh. 20. The increase in return is $70,467 times 6%		4,228
Increase in return due to use of year 1952 average Gas Plant Held for Future Use:		
Average Gas Plant Held for Future Use for 1952 per Sch. A–17	269,213	
Two year average used in Sch. 3, Exh. 20	161,232	
Increase in rate base	107,981	
Increase in return ($107,981 times 6%)		6,479
Total Increases		10,707
Staff Adjustment (Net Decrease)		$ 274,666

(Here follows Exhibit 28, folios 437-440 and Exhibit 30, folios 441-548)

[fols. 437–440]

EXHIBIT 28

TABLE NO. II

Docket No. G–1115

Colorado Interstate Gas Company

Summary—Allocation of Cost of Service

Total System
Year 1952—Estimated

Line	Customer and Class of Sale	Annual Volume Mcf [1]	Revenue	Cost of Service				Excess Revenue Over Cost of Service	Average Revenue Cents/Mcf [1]	Average Cost Cents/Mcf [1]
				Production	Transmission	Distribution [2]	Total			
	(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
	Transmission System									
	Sales to Other Utilities									
	Jurisdictional									
1	G–1 Rate Schedule	66,179,300	$10,747,115	$2,424,316	$5,264,683	$131,894	$7,820,893	$2,926,222	16.24	11.82
2	G–2 Rate Schedule	264,000	45,288	9,673	22,268	2,997	34,938	10,350	17.15	13.23
3	P–1 Rate Schedule	16,482,000	2,187,885	603,768	1,239,682	20,696	1,864,146	323,739	13.27	11.31
4	I–1 Rate Schedule	2,953,700	369,213	108,196	193,345	8,917	310,458	58,755	12.50	10.51
5	I–2 Rate Schedule	[3]	[3]	—	—	—	—	—	—	—
6	Clayton Gas Company	240,000	35,160	8,768	24,481	2,975	36,224	(1,064)	14.65	15.09
7	Total Jurisdictional	86,119,000	13,384,661	3,154,721	6,744,459	167,479	10,066,659	3,318,002	15.54	11.69
	Non-Jurisdictional									
8	Dalhart Gas Company	535,000	72,225	19,603	51,647	6,000	77,250	(5,025)	13.50	14.44
9	Total Sales to Other Utilities	86,654,000	13,456,886	3,174,324	6,796,106	173,479	10,143,909	3,312,977	15.53	11.71
10	Direct Sales—Non-Jurisdictional	15,958,000	2,135,721	584,565	1,038,397	35,357	1,658,319	477,402	13.38	10.39
11	Total Transmission System Sales	102,612,000	15,592,607	3,758,889	7,834,503	208,836	11,802,228	3,790,379	15.20	11.50
	Leased Transmission System									
	Jurisdictional									
12	Natural Gas Pipeline Co. of America	48,051,000	1,945,400	1,760,213	443,000	52,544	2,255,757	(310,357)	4.05	4.49
	Field System									
	Non-Jurisdictional									
	Amarillo Oil Company									
	Contract "B"									
13	Well Mouth	6,323,000	133,785	179,309		15,465	194,774	(60,989)	2.12	2.08
14	Gathering	7,682,000	181,745	322,753		12,862	335,615	(153,870)	2.37	4.37
15	Total Contract "B"	14,005,000	315,530	502,062		28,327	530,389	(214,859)	2.25	3.79
16	Contract "C"—Gathering	112,000	9,005	4,684		2,857	7,541	1,464	8.04	6.73
17	Total Amarillo Oil Co.	14,117,000	324,535	506,746		31,184	537,930	(213,395)	2.30	3.81
18	Other Field Sales	1,355,000	99,990	56,951		13,640	70,591	29,399	7.38	5.21
19	Total Field System Sales	15,472,000	424,525	563,697		44,824	608,521	(183,996)	2.74	3.93
20	Total All Sales	166,135,000	$17,962,532	$6,082,799	$8,277,503	$306,204	$14,666,506	$3,296,026	10.81	8.83
	Recapitulation									
21	Jurisdictional	134,170,000	15,330,061	4,914,934	7,187,459	220,023	12,322,416	3,007,645	11.43	9.18
22	Non-Jurisdictional	31,965,000	2,632,471	1,167,865	1,090,044	86,181	2,344,090	288,381	8.24	7.33
23	Total System Sales	166,135,000	$17,962,532	$6,082,799	$8,277,503	$306,204	$14,666,506	$3,296,026	10.81	8.83

[1] Pressure Base 14.65 p.s.i.a.
[2] Distribution Costs Allocated 50% Commodity—50% Customer
[3] The small amount of I–2 gas has been included under G–1
( ) Indicates Negative Figure

EXHIBIT 30

SCHEDULE No. 1

Colorado Interstate Gas Company

Estimated Cost of Service and Deficiency in Revenues as Estimated for Year 1952

Line No.		Total (1)	Production								Hugot	
			Total Production (2)	Panhandle Field								
				Well Mouth (3)	Gathering (4)	Fourway Dehydration (5)	Fourway Gasoline (6)	Bivins Gasoline (7)	Fritch Gasoline (8)	Gas Purchased (9)	Well Mouth (10)	
1	Gas Service Revenues (Sch. 3)	$17,962,532										
2	Cost of Service											
3	Operating Revenue Deductions											
4	Gasoline Net Revenues (Sch. 5)	(583,324)	($ 583,324)	$	$	$	($109,978)	($228,319)	($39,920)	$	$	
5	Other Gas Revenues—Rent (Sch. 4)	(37,500)	(3,450)				(1,250)	(2,200)				
6	Production Expenses											
7	Gas Purchased (Sch. 6)	2,082,000	2,082,000							2,082,000		
8	Gas Used in Operations (Sch. 6)	(270,300)	(270,300)	(167,100)							(103,200)	
9	Other Production Expenses (Sch. 7)	2,018,250	2,018,250	1,642,304	100,243	5,058					146,427	
10	Transmission Expenses											
11	Operation and Maintenance (Sch. 7)	2,507,120										
12	Rental of Leased Facilities (Sch. 7)	443,000										
13	Distribution Expenses (Sch. 7)	173,303										
14	Administrative and General (Sch. 7)	1,808,611	604,888	285,475	100,735	6,182	34,184	10,663			6,001	
15	Sub-Total	8,141,160	3,848,064	1,760,679	200,978	11,240	(77,044)	(219,856)	(39,920)	2,082,000	49,228	
16	Depreciation (Sch. 8)	2,678,673	903,868	375,286	153,373	10,200	57,707	26,440			9,936	
17	Depletion (Sch. 9)	57,688	57,688	57,688								
18	Taxes—Federal Income (Sch. 10)	2,306,808	293,595	(312,211)	170,165	11,383	64,373	29,739			25,717	
19	—State Income (Sch. 11)	63,765										
20	—Other (Sch. 12)	1,835,229	1,174,095	420,000	628,659	3,397	18,775	11,185			3,295	
21	Total Operating Revenue Deductions	15,083,323	6,277,310	2,301,442	1,153,175	36,220	63,811	(152,492)	(39,920)	2,082,000	88,176	
22	Return at 6.5%	3,718,028	1,276,183	539,286	206,806	13,885	78,329	36,158			31,378	
23	Total Cost of Service	$18,801,351	$7,553,493	$2,840,728	$1,359,981	$50,105	$142,140	($116,334)	($39,920)	$2,082,000	$119,554	
24	Deficiency	($ 838,819)										

EXHIBIT 30

SCHEDULE No. 1

Colorado Interstate Gas Company

Estimated Cost of Service and Deficiency in Revenues as Estimated for Year 1952

	Production										Transmission			
	Panhandle Field					Hugoton and Loveland Fields								
	l Mouth (3)	Gathering (4)	Fourway Dehydration (5)	Fourway Gasoline (6)	Bivins Gasoline (7)	Fritch Gasoline (8)	Gas Purchased (9)	Well Mouth (10)	Gathering (11)	Lakin Dehydration (12)	Lakin Gasoline (13)	Total Transmission (14)	Bivins Dehydration (15)	Other (16)	Total Distribution (17)
		$	$	($109,978)	($228,319)	($39,920)	$	$	$	$	($205,107)	$	$	$	$
				(1,250)	(2,200)							(34,050)		(34,050)	
	(67,100)						2,082,000								
	542,304	100,243	5,058					(103,200) 146,427	118,903	5,315					
												2,507,120	27,840	2,479,280	
												443,000		443,000	
	85,475	100,735	6,182	34,184	10,663			6,001	137,647	6,182	17,819	1,189,722	5,273	1,184,449	173,303
	60,679	200,978	11,240	(77,044)	(219,856)	(39,920)	2,082,000	49,228	256,550	11,497	(187,288)	4,105,792	33,113	4,072,679	14,001
	75,286	153,373	10,200	57,707	26,440			9,936	229,716	10,384	30,826	1,755,598	9,663	1,745,935	187,304
	57,688														19,207
	12,211)	170,165	11,383	64,373	29,739			25,717	257,957	11,720	34,752	1,989,119	11,013	1,978,106	24,094
	20,000	628,659	3,397	18,775	11,185			3,295	75,601	3,396	9,787	63,765 653,444	2,896	63,765 650,548	7,690
	01,442	1,153,175	36,220	63,811	(152,492)	(39,920)	2,082,000	88,176	819,824	36,997	(111,923)	8,567,718	56,685	8,511,033	238,295
	39,286	206,806	13,885	78,329	36,158			31,378	313,771	14,186	42,384	2,412,940	13,363	2,399,577	28,905
	40,728	$1,359,981	$50,105	$142,140	($116,334)	($39,920)	$2,082,000	$119,554	$1,133,595	$51,183	($ 69,539)	$10,980,658	$70,048	$10,910,610	$267,200

[fol. 549] BEFORE THE FEDERAL POWER COMMISSION
Items by Reference

Ite. A

March 16, 1951.

United States of America, Federal Power Commission. In the Matter of Colorado Interstate Gas Company and Canadian River Gas Company. Docket No. G-1326.

Before Commissioners: Mon C. Wallgren, Chairman; Thomas C. Buchanan, Claude L. Draper, Nelson Lee Smith and Harrington Wimberly.

OPINION No. 209

On March 1, 1951, we authorized Colorado Interstate Gas Company (Colorado) to acquire by merger and to operate all of the properties of Canadian River Gas Company (Canadian) which are subject to our jurisdiction. This we did by order without opinion, since we thought that preparation of an opinion would unduly delay the beginning of construction of the pipeline facilities proposed, contingent upon our approval of the merger, to be built by Colorado, and which are sorely needed to augument the supply of natural gas available to Denver, Cheyenne and the Rocky Mountain area. We thought also that the project, considered as a whole, was so plainly desirable in the public interest that a detailed exposition of our views was unnecessary.

On March 6, 1951, however, Commissioner Buchanan, who dissented from our order, filed a dissenting opinion which, by unjustified insinuation and intemperate assertion, violently assails our action and, in effect, the Commisioners who took part in it. Therefore, we think it proper to set out fully the reasons for our decision and the processes by which we arrived at it.

Our duty is to weigh carefully and fairly all of the evidence in each case which comes before us to the end that we may arrive at the true facts assembled in their proper re-

lation. We must consider impartially the inferences from these facts that are urged upon us by contending parties, [fol. 550] and, by the exercise of our own judgment, decide upon the action which will advance the purposes of the Congress as embodied in the statutes which we must administer.

It would be unnecessary to set out these obvious principles were it not that the dissenter has, in our opinion, departed from them. He has accepted, apparently without question, all of the evidence and all of the conclusions of one of the two contending parties. As a result, his opinion necessarily has been cast in the mold of a partisan brief, giving a distorted, rather than a factual, picture of the situation. Our reference to "the two contending parties" is to the applicants and to our staff which strongly opposed Colorado's proposal, as it was free to do.[1] However, when our staff assumes an adversary position in a formal proceeding, its evidence and contentions must receive no preferred consideration by reason of their origin.

Commissioner Buchanan has accused us of placing upon the gas consumers of Denver, Cheyenne and the Rocky Mountain area "an unreasonable and unconscionable burden" which, he says, approximates $800,000 a year. Whether this is so depends upon the validity of his assumptions and conclusions and upon the proper disposition of all the problems presented to us by this case. Paramount is [illegible] on the problem of how best to assure natural-gas service at reasonable rates to consumers dependent upon Colorado's pipeline.

In order to have a clear understanding of the matters presented and considered by the Commission, it is necessary to review historically the relationship between Colorado and Canadian. In 1927, a decade before the Natural Gas Act was passed, Southwestern Development Company (Southwestern) through a subsidiary, Amarillo Oil Company (Amarillo), owned almost 300,000 acres of gas and

[1] Other parties were: Natural Gas Pipeline Company of America; City of Colorado Springs, Colorado; Public Service Company of Colorado; City and County of Denver, Colorado.

oil lands on which there were then about 10 producing gas wells and some gathering pipelines. Cities Service Com-[fol. 551]pany (Cities Service), through two subsidiaries, then owned manufactured gas distribution facilities in the cities of Denver and Pueblo, Colorado, and engaged to and did secure new franchises for the distribution of natural gas in those cities.

To link the gas lands with the markets, a three-way transaction was made between Southwestern, Standard Oil Company of New Jersey (Standard Oil) and Cities Service with the ultimate objective of building a pipeline from the West Panhandle Gas Field to Denver and beyond. Southwestern organized a new corporation called Canadian River Gas Company with all of its capital stock (except qualifying shares) going to Southwestern, which then had its subsidiary, Amarillo, convey all of its gas lands and facilities to Canadian. Canadian then issued $11,000,000 in bonds secured by mortgage upon all of its property, and the bonds were bought by Colorado, which had been organized by Standard Oil at the time Canadian was organized for the purpose of building the pipeline to Denver. The proceeds of the Canadian bond issue were used, first to pay Amarillo $5,000,000 for the gas lands and facilities conveyed to Canadian, and then to finance the drilling of additional wells and the construction of additional necessary facilities for delivery of gas to Colorado Interstate at Clayton, New Mexico. Amarillo reserved certain priorities of service of gas produced from the reserves for the benefit of itself and certain other Texas customers.

Contemporaneously, a "cost contract" was made between Canadian and Colorado, but Canadian first exacted as a consideration for entering into such cost contract the issuance and delivery to it (or its nominee) of 42½% of Colorado's common stock (par value $1,000,000) and also one-half of Colorado Interstate's preferred stock (par value $1,000,000).

Under the contract Colorado is obligated to put up all the money Canadian needs for all of its out-of-pocket costs and the building of its facilities, and Canadian owns and will continue to own all of its facilities and gas reserves.

Colorado loans this money for these purposes and is repaid by Canadian over varying periods of time in effect under the contract. Canadian gets its money for such repay- [fol. 552] ment from its sales of gas to Colorado and the Texas customers, but gets to keep no more money than the amount required to meet out-of-pocket financial obligations. These payments of debt to Colorado, along with operating expenses, are the amounts of money which Canadian charges for its gas. Since 1945, however, when the rate order of this Commission[2] against Canadian was finally made effective, the price of gas to Colorado has no longer been computed on the actual cost basis fixed by the contract, but is fixed at 4¢ Mcf for that delivered to Colorado at Clayton, New Mexico, and 3½¢ per Mcf for that which is ultimately delivered to Natural Gas Pipeline Company of America. If the money secured from these rates does not produce sufficient cash, together with Canadian's other receipts, to pay all out-of-pocket expenses and costs, including interest on and repayment of loans, Colorado must make a "below-the-line" payment to Canadian to make up the deficiency. On the other hand, if Canadian through the collection of revenues from its various sales of gas collects more that what is necessary to meet its cash obligations, that is paid by Canadian as "other income" to Colorado and is also accounted for below the line. By the expression "below-the-line" is meant that such payments by Colorado, and such receipts by it, are not operating expenses or operating revenues.

Although under this cost contract Colorado pays for all of Canadian's production, gathering and transmission facilities, Colorado cannot pledge any of these properties as security for funded debt.

Southwestern set up its investment in Canadian's stock at $1.00 on its books and has never revalued that stock. Under Article Fifth of the cost contract, it was also provided that the gas to be delivered by Candian to Colorado should be "natural gas as produced in its natural state

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[2] In the Matter of Canadian River Gas Company, Colorado Interstate Gas Company, 3 FPC 32 (1942).

from the wells, except that Canadian may extract or permit the extraction of natural gasoline from its natural gas, * * *" but that such extraction should not subject the nat- [fol. 553] ural gas to a change in the chemical composition of any of its component parts, or which might dilute the natural gas.

The value of the ownership by Southwestern of Canadian's stock is due in part to certain tax benefits arising by virtue of the filing of consolidated Federal income tax returns since Canadian is a wholly-owned subsidiary of Southwestern. In addition to the tax benefits, there are also reversionary rights that mature after the expiration of the cost contract to the beneficial interest, in all of Canadian's assets.

The cost contract by its terms would continue just so long as Canadian had available for deliv[illegible]y to Colorado quantities of natural gas which Colorado determined were profitable for it to buy under the terms of the cost contract, or until such time as the volume of gas available from Canadian production is sufficient only to supply the requirements of the Texas markets, which have priority over Colorado. The record indicates that this probably will occur by 1972. Canadian would then own, free from the provisions of the cost contract all of the facilities previously constructed and paid for with funds received from Colorado under the terms of the cost contract, together with the remaining gas reserves Further, the record indicates that continued deliveries of gas to Canadian's Texas customers would then be feasible.

It was in the light of this background that Colorado and Canadian in February 1950 filed a joint application (amended in April 1950) under Section 7 of the Natural Gas Act for authority for Colorado (1) to acquire and operate all of Canadian's properties and facilities presently used for the transportation or sale of natural gas subject to the jurisdiction of the Commission, and to perform the services now carried on by both companies; and (2) contingent upon approval of such acquisition, to construct certain new transmission lines and appurtenant facilities so as to materially increase the delivery capacity of Colorado's transmission

system to meet the progressively increasing demands of Colorado's customers and their consumers in the Rocky [fol.554] Mountain area.

This application was based upon an agreement between Southwestern and Colorado under which Southwestern will transfer all of the stock of Canadian to Colorado, which will thereupon cancel the Canadian stock and effect a merger of the two corporations, which automatically will end the cost contract. In consideration for Canadian's stock, Colorado will grant to Southwestern all of the natural gasoline contained in the natural gas in Canadian's acreage, but subject to continued deliveries of raw gas by Colorado to Amarillo and other Texas customers which Canadian is now contractually obligated to make, reserving however such gasoline as is contained in the gas which Colorado will deliver to its customers, the gasoline involved in minor deliveries of raw gas which Colorado may in its judgment hereafter make in the producing field, and gasoline represented by prior royalty interests. Colorado undertakes to extract, in accordance with Southwestern's specifications, the gasoline content of the natural gas, derived from Canadian's acreage, which supplies Colorado's Clayton-Denver line, and to deliver such gasoline to Southwestern at Colorado's Bivins Extraction Plants. Southwestern will market the gasoline at its own expense, which is estimated to be ¼¢ per gallon, and pay over to Colorado an amount equal to 50% of the gross revenues to compensate Colorado for the estimated costs of producing, gathering and extracting the natural gasoline. Colorado further agrees to give Southewestern 85% of the net revenues due to Colorado from the operation of Texoma Natural Gas Company's Fritch plant, where gasoline is extracted from the gas delivery by Colorado to supply one-fourth of the requirements of Natural Gas Pipeline Company of America. Out of its share of the gasoline revenues Colorado will make all royalty payments related to the total gasoline production from Canadian's acreage.

From the evidence adduced during the hearings it appeared that the present and future demands for gas of Colorado's customers in the Denver-Wyoming area had

increased to a point where existing transmission facilities [fol. 555] were inadequate to transport the needed additional gas for this area. Colorado's proposal for the construction of a new transmission line with appurtenant facilities provided for a 20-inch pipeline 215 miles in length, extending from a point in the West Panhandle Field northward to connect near Kit Carson, Colorado, with Colorado's existing pipeline from the Kansas-Hugoton Field to the Denver market. The cost of these new facilities was estimated at about $10,000,000, and the evidence also disclosed that Colorado's supplier of gas, Canadian, required about $3,500,000 to defray the cost of drilling new wells in order to augment its supply of gas so as to meet the increasing demands of Colorado.

It was also shown on the record that Colorado had then borrowed approximately $19,000,000 against its net plant of $30,175,887, which was close to the limit to which it could borrow under the loan indenture which restricts its borrowing to two-thirds of its net plant.

Due to this limitation upon its borrowing power, Colorado maintained that it was unable to finance the construction of the new pipeline between the Panhandle Field and its existing transmission line connecting the Kansas-Hugoton Field with the Denver market so as to serve adequately the needs of the consumers in the Colorado and Wyoming Rock Mountain area. Its proposal to acquire the properties and facilities of Canadian, and then to merge them into one integrated operating company, appeared to the Commission to be clearly in the public interest and, after briefs had been filed and oral argument had, the Commission, without any dissent, entered an order on July 20, 1950, to that effect, but reopened the proceeding for further evidence upon the sole question of the reasonableness of the consideration to be paid to Southwestern.

Before beginning a detailed discussion of the natural gasoline revenues and tax benefits or losses which are involved in consideration of this case there should be emphasized that the evidence of record relating to these subjects necessarily consists of estimates and forecasts. From the very nature of the subject matter it is impossible with

[fol. 556] certainty to arrive at precise or assured conclusions. The most that we or anyone else can do is to judge the validity of methods used and the reasonableness of estimates produced.

The essence of the contentions expressed in the dissent is that the project will cost Colorado's rate payers a sum which Commissioner Buchanan variously states as $18,087,128, $20,000,000 and $22,500,000. In our view, the record supports the conclusion that, based upon the best estimates available and an assumed average price for natural gasoline of 5¢, the gross gasoline revenues which Southwestern will receive will total $18,087,128 for a 23-year period extending through 1972.[3] Income taxes which must be paid on this sum by Southwestern will, at current rates, reduce it to $9,947,920.

The figure of $22,500,000, advanced by Commissioner Buchanan as the approximate total payments to Southwestern by reason of the transaction, is based upon an assumption that gas will be available from the Canadian acreage for Colorado's Clayton-Denver line after 1972. We think that this assumption is unfounded since the record shows that production from the Canadian acreage will probably have declined by 1972 to such a point that the volume of gas available therefrom will be sufficient only to supply the requirements of the Texas markets, which retain their priority over those in the Rocky Mountain area. Moreover, there will be no deliveries to the Natural Gas Pipeline Company of America after 1966. When such time comes Southwestern will cease to be entitled to any gasoline revenues from the extraction process carried on at the Bivins plant.

Dividing $18,087,128 by 23 gives an average annual gross revenue to Southwestern of $786,397 from gasoline produced by Colorado over the 23-year period from the Canadian acreage. We assume that Commissioner Buchanan

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[3] All figures based upon estimated gasoline revenues are overstated in the record, in the dissenting opinion and in this opinion since they include estimates for all of 1950 and 1951, whereas the merger cannot become effective until sometime later this year.

[fol. 557] rounded off this latter figure to reach his conclusion that our decision will deprive gas consumers of approximately $800,000 annually. However, to reach that conclusion he had to make a number of assumptions which we consider unjustified and to ignore certain admitted facts.

First it was necessary to assume that Colorado's present rates will yield at least $18,087,128 in revenues through 1972 in excess of a fair rate of return on investment, for otherwise the impact on Colorado of the gasoline revenue receipts relinquished must be reduced by the amount of the income taxes which would be paid thereon. This is indicated by the testimony of the staff accounting witness. We cannot and we think should not make such an assumption prior to hearing and final determination by us of the formal investigation now in progress of the rates of Colorado and Canadian (Docket No. G-1115). Should the prejudgment of the rate case indulged in by Commission Buchanan be proven incorrect by the Commission's ultimate decision, based upon a more exact and complete record than that in this proceeding, the net diminution of revenues to Colorado by reason of Southwestern's share of the gross gasoline proceeds will be something under the $18,087,128 figure and may range as low as $9,947,920, which latter figure is derived by deducting income taxes computed at the current rate from the gross figure of $18,087,128.

The $9,947,920 figure clearly represents the full benefit Southwestern can expect to receive from gasoline revenues accruing to it through 1972 by reason of the merger agreement. The weight of the evidence indicates that this gain will be offset in large part by a loss to Southwestern of tax benefits estimated at $7,305,000, by reason of its relinquishing its ownership of Canadian. Thus, the net gain to Southwestern from the transaction over the 23-year period, as closely as it can be determined from estimates in this record, will approximate $2,642,920. The tax benefits, on the other hand, which Southwestern will relinquish under the merger transaction result from the fact that, beginning in 1956, Canadian would have substantial income [fol. 558] tax credits which, but for the transfer of Canadian's stock, would be available on a consolidated tax re-

turn to its parent, Southwestern. These and other credits now will be -vailable to Colorado.

Commissioner Buchanan has sought to show tax benefits which Southwestern is foregoing will be $2,238,282 less than the estimate which we consider to be supported by the record. He bases this contention solely upon the assumed tax impact of the recent case of Hudson, et al. v. Commissioner of Internal Revenue, 11 U. S. Tax Appeals 1042, affirmed per curiam, 183 F. (2d) 180 F. (2d) 180 (5th Cir.), which is claimed to establish that Southwestern, rather than Colorado, will be entitled to percentage depletion allowance associated with production of natural gasoline from the Canadian reserves.

Aside from the doubtful applicability of the Hudson case to the factual situation before us, we think that the dissenter's contention in this regard can be disposed of shortly and completely by pointing out that the Commissioner of Internal Revenue has officially stated his non-acquiescence in the Hudson decision. This, we understand, means that the case will not be followed by the Bureau of Internal Revenue in administration of the tax laws. Thus, it is probable that the $2,238,282 percentage depletion allowance, said to depend upon whether or not the Hudson case is followed as a precedent, will not be available to Southwestern without litigation. And Southwestern's formal assurance to the Commission that, if it becomes entitled to percentage depletion for gasoline extracted by Colorado it will agree to pass on to Colorado its resulting tax savings, satisfies us that it will not attempt by litigation to obtain for itself the percentage depletion benefits expected to accrue to Colorado from the production of gasoline from the Canadian acreage.

Of far greater importance, however, than the extent to which Southwestern will benefit or lose from the merger transaction is the impact of the merger on the rate payers supplied with natural gas through Colorado's facilities. We already have demonstrated that the estimated $18,087,128 gross gasoline revenues which Colorado will give [fol. 559] up to Southwestern through 1972 cannot be assumed, in the absence of final determination of our rate

case, to be the net diminution in Colorado's revenues. This may range anywhere from that figure down to $9,947,920.

As against this cost Colorado stands to gain an estimated $14,324,415 in tax benefits becoming available to the merged company by reason of the transfer to it of the percentage depletion allowance based on the production of both natural gasoline and natural gas from Canadian's acreage. We think that the weight of the evidence supports this forecast in tax savings. Such savings clearly inure to the benefit of Colorado's customers and the consumers of the Rocky Mountain area.

Commissioner Buchanan attacks this estimate of tax benefits expected to accrue to Colorado on the basis of the Hudson case, which we already have discussed, and by giving no weight whatever to the evidence that there is a lieklihood that the percentage depletion allowance available to the merged company will be computed upon a wellhead gas valuation of 5¢ per Mcf rather than the current 3.17¢ valuation. The uncontradicted evidence, however, shows that other companies in the area where Canadian's reserves are located, whose operations are substantially similar to those to be undertaken by the merged company, have received approval of percentage depletion allowances based upon wellhead gas valuations of 5¢ per Mcf. The evidence shows that the comparatively low wellhead valuation accorded Canadian's gas probably has resulted from the proximity of the point of sale of the gas to Colorado to the producing field. This conclusion gains support from Section 29.23(m)-1 of the Commissioner's Regulations 111 which provides:

"In the case of oil and gas wells, 'gross income from the property' as used in section 114(b) (3) means the amount for which the taxpayer sells the oil and gas in the immediate vicinity of the well. If the oil and gas are not sold on the property but are manufactured or converted into a [fol. 560] refined product prior to sale, *or are transported from the property prior to sale, the gross income from the property shall be assumed to be equivalent to the representative market or field price (as of the date of sale) of the oil and gas before conversion or transportation.*" [Emphasis supplied.]

Further, the staff's accounting witness testified that he did not consider the 5¢ wellhead figure to be unreasonable. We cannot and do not here attempt to influence the depletion allowance ruling which will be made by the Bureau of Internal Revenue, but, from this record, we think that the basis upon which the tax savings to Colorado of $14,324,415 was estimated is a reasonable one.

Considerable significance is attributed in the dissent to the fact that the Administration has recommended to the Congress that the present depletion allowances of 27½% of the value at the wellhead be reduced to 15%. It is stated that this would drastically reduce the tax benefits to Colorado from the merger. But we cannot, if we are to be realistic, base any conclusions upon this proposed amendment of the tax laws. It would be just as reasonable for us to assume that the corporate income tax rate will be increased from 45% to 55%, as also has been recommended by the Administration. Such an assumption would greatly increase Colorado's prospective tax savings.

To sum up the probable cost and offsetting tax benefits to Colorado from the merger: Colorado will relinquish net revenues over a 23-year period which, based on estimates which appear to us to be reasonable, may possibly be as much as $18,087,128 or as little as $9,947,920,[4] depending upon the outcome of our formal rate case. Offsetting this will be estimated positive tax benefits, computed upon bases which we consider reasonable, of $14,324,415. Thus, laying aside for the moment all consideration of improved corporate structure, acquisition of physical property, enhancement of borrowing ability and the making available to the [fol. 561] gas consumers of the Rocky Mountain area of adequate supplies of low priced gas, the merger can be expected to involve at the most a cost to Colorado of $3,762,713 spread over a 23-year period, or, in its most favorable light, cash benefits to Colorado over the same period of $4,376,495.

These are the revenue figures which reasonably can be

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[4] The spread between these two figures represents 45% income tax on the larger, as explained above.

expected to have an effect upon Colorado's rates. Yet Commissioner Buchanan stated: "The revenues of more than 20 million dollars given up by Southwestern must be made up by the gas consumers for the reason that their cost of gas is increased by an equivalent amount since they enjoyed the credit in the past but will not have it in the future."

By this groundless conclusion the dissenter completely ignores that a very substantial tax saving will accrue to Colorado by reason of the merger, a fact which was freely admitted by the principal witness opposing the joint application. This witness sought only to show that the tax saving would be less than the amount claimed.

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Upon the record before us, we are convinced that the long-run benefits to the consumers dependent upon Colorado would far out-weigh any costs which could reasonably be expected to follow from the merger. However, to avoid any possible doubt as to the full protection to the gas consumers dependent on Colorado, we conditioned our certificate to provide (1) that any excess of cost to Colorado from its gasoline extraction operations over the revenues accruing to it therefrom, would not be considered as a cost of service to the company's natural-gas consumers and customers; (2) that Colorado should tender to its resale customers service agreements in which it would commit itself not to dispose of the natural-gas reserves to be acquired from Canadian so long as it is economically feasible to produce natural gas from such reserves; and (3) that it would tender to its resale customers service agreements in which it would commit itself not to propose any increase in any resale rate attributable in whole or in part to the acquisition and merger authorized by the certificate. We [fol. 562] also required that Colorado file with the Commission within 30 days its written acceptance of the certificate as conditioned.

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Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investi-

gation should be brought to a speedy conclusion. In our order issued March 1, 1951, we required Colorado, within four months of that date, to report to us the completion of the acquisition, the commencement of operation by it of facilities acquired, and proof of dissolution of Canadian. Therefore, we have, by order entered today, fixed the date of hearing in the rate case for August 1, 1951, which is one month after the required -ate for such report.

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BUCHANAN, Commissioner dissenting:

I find it necessary to dissent from the decision of the majority [1] in the above docket, because (1) in my opinion the decision unjustifiably deprives the gas consumers of Denver, Cheyenne and the Rocky Mountain area of a saving in gas rates of approximately $800,000 on an annual basis; and (2) the decision is completely at odds with fundamental principles of regulation vigorously espoused by this Commission and approved by the United States Supreme court.[2]

Since the majority, in their order, did not set forth their reasons for approving the Applicants' proposition or state why they found that the merger of Canadian and Colorado is required by the present public convenience and necessity or why, in their opinion, the payments proposed to be made by Colorado to Southwestern Development Company are reasonable and not incompatible with the public in- [fol. 563] terest, it is fair to assume that the majority have accepted as valid the reasons given by the joint Applicants why their proposal should be approved. It is, therefore, necessary for me to set forth in some detail the proposal of the Applicants, and the issues raised during the course of several hearings and in the briefs and oral argument.

Upon analysis, these alleged tax benefits appear extremely indefinite and uncertain. They are based upon the

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[1] Order date February 28, 1951.

[2] Canadian River Gas Co. v. F. P. C., et al., 324 U. S. 581.

unwarranted assumption that the Bureau of Internal Revenue will increase from 3.17¢ per Mcf to 5¢ per Mcf the gross value at the wellhead of natural gas used in computing Canadian's statutory depletion allowance. The 5¢ value was developed by Southwestern's auditor and represents his sole judgment (T. 1128). Furthermore, the record shows (T. 1136) that the sale of gas at the Fritch Plant between Colorado and Natural Gas Pipe Line Company at 3½¢ per Mcf will continue after the merger. In the face of these facts and of the great need of the Federal Government for revenue at this time it does not seem reasonable nor possible to assume that the Government is going to give up tax revenues amounting to $300,000 a year simply because of the elimination of the interdepartmental sale between Canadian and Colorado through a merger.

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[fol. 564] BEFORE THE FEDERAL POWER COMMISSION

ORDER ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY AUTHORIZING ACQUISITION AND OPERATION OF PIPELINE FACILITIES AND AMENDNG ORDER ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY AUTHORIZING CONSTRUCTION OF NEW PIPELINE FACILITIES—Issued March 1, 1951

Upon further consideration of the joint application filed by Colorado Interstate Gas Company (Colorado) and Canadian River Gas Company (Canadian) on February 13, 1950, as amended on April 4, 1950. for certificates of public convenience and necessity authorizing (a) the acquisition and operation by Colorado of all the properties and facilities of Canadian, and (b) the construction and operation by Colorado of additional pipelines and facilities, it appears from all evidence adduced at the public hearings in this proceeding, the briefs of all counsel submitted at the conclusion of the hearings, and oral argument, that:

On July 20, 1950, following public hearing, submission of briefs, and after the conclusion of oral argument in the above entitled proceeding, the Commission issued a certificate of public convenience and necessity authorizing

Colorado and Canadian to construct and operate certain natural-gas pipeline facilities as fully described in the amended joint application mentioned in the last preceding paragraph.

By said order of July 20, 1950, the Commission found that a merger of the facilities and properties of Canadian with the facilities of Colorado was in the public interest and by paragraph (B) thereof reopened the proceeding for hearing at a date to be fixed by the Commission for testimony limited to the sole issue of the reasonableness of payments proposed to be paid to Southwestern Development Company by Colorado for the acquisition of Canadian's properties and facilities.

Thereafter said order of July 20, 1950, was amended by order dated October 3, 1950, so as to extend to December 20, 1950, the time within which to submit their plan for financing, satisfactory to the Commission, to defray the cost of constructing such proposed additional facilities. [fol. 565] Pursuant to the Commission's order of November 1, 1950, fixing the time and place of further public hearings herein, evidence has been adduced respecting the reasonableness of the contemplated payments by Colorado to Southwestern Development Company, and of respecting the financing plan of Colorado.

The Commission finds:

(1) All of the properties and facilities proposed to be acquired and operated by Colorado from Canadian, as described in said joint application, as amended, will become and be an integral part of the presently owned and operated properties and facilities of Colorado and will thereafter be used for the transportation and sale of natural gas in interstate commerce, subject to the jurisdiction of the Commission, and such acquisition and operation thereof as an integral part of the pipeline system presently owned and operated by Colorado are subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act, as amended.

(2) The Commission's order of July 20, 1950 should be amended so as to allow Colorado additional time within

which to commence and complete the construction of the additional pipe lines and appurtenant facilities which were authorized by the Commission's order of July 20, 1950.

(3) Colorado has secured a firm and binding commitment from a responsible lender for a loan of $12,000,000 at an interest rate of 2⅞ percent, conditioned, however, on the consummation of the acquisition by Colorado of Canadian's properties and facilities, the proceeds of which loan will be reasonably adequate to enable Colorado to finance the construction of the additional pipe lines and appurtenant facilities authorized by the Commission's order of July 20, 1950.

(4) Such acquisition will not adversely affect Colorado's supply of gas and will permit Colorado to better serve its customers at present rates. Colorado is able and willing properly to do the acts and to continue to perform all existing services of both companies and to conform to the provisions of the Natural Gas Act, as amended, and the [fol. 566] requirements, rules and regulations of the Commission thereunder.

(5) The acquisition and operation by Colorado of all of the properties and facilities presently owned and operated by Canadian, as they are described in said amended joint application, through the acquisition of all of the capital stock of Canadian from Southwestern Development Company, and the contemporaneous corporate merger of the two operating companies, is required by the present public convenience and necessity.

(6) The payments proposed to be made by Colorado to Southwestern Development Company as the consideration for all of the capital stock of Canadian is reasonable and not incompatible with the public interest and such acquisition should be approved, as hereinafter conditioned.

The Commission orders:

(A) A certificate of public convenience and necessity be and the same is hereby issued authorizing Colorado to acquire and operate the properties and facilities presently owned by Canadian and described in the amended joint application (together with the exhibits therein mentioned and made a part thereof) for the transportation and sale of

natural gas as therein set forth, subject to the jurisdiction of the Commission, upon the following terms and conditions:

(i) The authorization herein granted for effectuating the acquisition and operation of Canadian's properties and facilities is upon the express understanding and condition that if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritsch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pur-[fol. 567] suant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers.

(ii) Colorado shall, within 4 months from the date of this order, report to the Commission in writing, under oath, the completion date of the acquisition hereby authorized and also the date at which it commences operation of the facilities so acquired, together with a duly authenticated certificate or other document showing the final dissolution of Canadian River Gas Company by the surrender of its corporate charter.

(iii) The entries in Colorado's books of account respecting the cost of all properties and facilities acquired by it by reason of this certificate shall be subject to the approval of this Commission.

(iv) Colorado shall tender to all of its resale customers service agreements in which Colorado will agree (1) that it will not sell, transfer or otherwise alienate natural gas reserves which it proposes, as part of the acquisition and merger, to acquire from Canadian, so long as it is economically feasible to produce natural gas from such reserves, and (2) that it will not propose any increase in any

rate subject to the jurisdiction of the Commission which will be attributable in whole or in part to the acquisition and merger authorized herein.

(v) Colorado shall, within 30 days from the date hereof, file with this Commission a certificate duly authorized by its Board of Directors and duly executed by its executive officers, showing the acceptance of this certificate of public convenience and necessity.

(B) Colorado shall commence the construction of the new additional facilities involved in this proceeding (described in the amended joint application) within six months from the date of the issuance of this order and shall complete such construction within one year from the date hereof.

[fols. 568-592] (C) Colorado shall submit to the Commission, in writing, commencing six months from the issuance of this certificate monthly progress reports which shall generally include statements concerning the purchase of material and equipment and the progress of the construction work, and upon completion advise the Commission of the completion date, together with the date of commencement of operations.

(D) This certificate is not transferable and shall be effective only so long as Colorado continues the services and operations hereby authorized in accordance with the provisions of the Natural Gas Act, as amended, and any pertinent rules, regulations or orders heretofore or hereafter issued by the Commission.

By the Commission. Commissioner Buchanan dissenting and will file a separate statement.

J. H. Gutride, Acting Secretary.

* * * * * * *

And thereafter the following proceedings were had in said cause in the United United States Court of Appeals for the Tenth Circuit:

Order: Cause Argued and Submitted.

First Day, September Term, Tuesday, September 8th, 1953. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard, James Lawrence White, Esquire, and William A. Daughtery, Esquire, appearing for petitioner, Jacob Goldberg, Esquire, appearing for respondent.

On motion, the City of Colorado Springs, Colorado, was granted leave to intervene in this cause.

Thereupon this cause was argued by counsel and was submitted to the court.

OPINION

[Oct. 29, 1953]

James L. White and William A. Dougherty (John P. Akolt, Sr., John R. Turnquist, Charles E. McGee and Lewis M. Poe were with him on the brief) for Petitioner;

Jacob Goldberg (Bradford Ross, Bernard A. Foster, Jr., and Reuben Goldberg were with him on the brief) for Respondent.

Before BRATTON, HUXMAN and MURRAH, United States Circuit Judges.

HUXMAN, Circuit Judge.

Colorado Interstate Gas Company, herein referred to as Colorado, a natural gas company under the Natural Gas Act, seeks review of the order of the Federal Power Commission, herein referred to as the Commission, entered under the appropriate provisions of the Act,[1] reducing Colorado's rate for natural gas sold in interstate commerce for resale. Nineteen hundred fifty-two was taken as the test period. Based upon Colorado's operations for that year, the Commission found and concluded that the rates established by Colorado in connection with interstate business were unjust, unreasonable and excessive and resulted in an unreasonable and excessive exaction from its customers in the sum of $3,111,187 and that new rates reflecting a reduction of such sum in such revenues would be just and reasonable. Such rates were ordered and this petition for review challenges the correctness and validity of such order.

In arriving at its conclusions, the Commission accepted for the test period of 1952 the total revenues of $19,104,052 as reflected by

[1] 15 U. S. C. A. § 717-717 (w).

Colorado's books and as used by it in its exhibits in the case. Colorado's books reflected a total rate base of $57,200,440, while the Staff used a total rate base of $57,164,666, only $35,794 less than shown by Colorado's books. No issue is raised with respect to this slight difference and it may be disregarded. Colorado's revenues for the year 1952 in the total sum of $19,104,052 were accepted by the Staff and by the Commission. Colorado claims a total cost of service of $19,942,871, while the Staff adopted a cost of service base of $15,549,802. The Commission adopted a cost service base of $14,952,567, of which it allocated $10,273,474 to jurisdictional operations. It adopted 5¾% as a fair rate of return and fixed new rates which it concluded would return to Colorado from jurisdictional operations $10,289,269.

Colorado owns and operates extensive natural gas production gathering and processing facilities in the West Panhandle Field of Texas and also purchases and processes large volumes of natural gas in the Hugoton Field of Kansas. It also owns and operates a transmission pipeline system, extending from such fields to its general market area at Denver, Colorado. Sales are made from such pipelines to distributing facilities for resale and to industrial customers.

This proceeding was instituted on the Commission's own initiative. Extensive and numerous hearings were held. Hearings began on October 1, 1951, before a presiding examiner of the Commission and with intervening recesses were concluded on April 4, 1952. By order of May 23, 1952, the Commission dispensed with the filing of the intermediate opinion of the trial examiner. Briefs were thereafter filed with the Commission. Arguments of counsel were had and on August 8, 1952, the Commission issued its opinion with an accompanying order, directing a reduction of rates as above outlined.

Numerous assignments of error are urged by Colorado. Among others, it contends that dispensing with the filing of the trial examiner's intermediate report constitutes deprivation of due process and voids the order of the Commission. Since this contention, if sustained, would dispose of the case and make unnecessary a consideration of the remaining assignments of error, we consider it first.

5 U. S. C. A. § 1007 (a) in part provides, "In cases in which the Agency has not presided at the reception of the evidence, the officer who presided * * * shall initially decide the case or the agency shall require * * * the entire record to be certified to it for initial decision. Whenever such officers make the initial decision and in the absence of either an appeal to the agency or review upon motion of the agency within time provided by rule, such decision shall without further proceedings then become the decision

of the agency. On appeal from or review of the initial decisions of such officers the agency shall, except as it may limit the issues upon notice or by rule, have all the powers which it would have in making the initial decision. Whenever the agency makes the initial decision wthout having presided at the reception of the evidence, such officers shall first recommend a decision except that in rule making or determining applications for initial licenses * * * (2) any such procedure may be omitted in any case in which the agency finds upon the record that due and timely execution of its functions imperatively and unavoidably so requires."

There are not many decided cases which have dealt with the power of the Commission to dispense with the trial examiner's initial report. In *Kenny* v. *United States*, 103 F. Supp. 971, a three-judge court held that under the Interstate Commerce Act the exceptions embodied in Section 1007 (a) (2) were intended to permit the omission of the intermediary report or tentative decision by a trial examiner where the law contemplated speedy and expeditious proceeding by the agency. While that case arose before the Interstate Commerce Commission under the Interstate Commerce Act providing that the Commission "shall give to the hearing and decision * * * preference over all other questions", we think what was said applies with equal force and logic under the Act in question here.[2] We think it is clear that Congress intended that party contestants before the Commission are as a matter of right entitled to the benefits of the intermediate report save only in the two exceptions noted in Section 1007 (a) (2) but we are of the further view that under the exceptions as noted the Commission may in the exercise of a sound discretion either upon its own volition or upon the application of any party to the proceeding dispense with the filing of the report. In Footnote 3 we have set out some of the

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[2] See also *Alabama-Tenn. Natural Gas Co.* v. *Federal Power Commission*, 203 F. (2d) 494.

[3] With respect to this exception, Congressman Walter, one of the co-authors of the bill, explaining the exceptions stated that "the parties will be better served if the proposed decision * * * reflects the views of the responsible officers in the agencies, whether or not they have actually taken the evidence." Senate Docket No. 248, 79th Congress, Second Session, Page 361.

And the Senate Committee said, "The exemption of rule making and determining initial applications for licenses from provisions of Section 5 (c), 7 (c), and 8 (a) may require change if, in practice, it developes that they are too broad. Earlier in this report in commenting upon some of those provisions, the Committee had expressed its reasons for the language used and had stated that,

expressions in Congress. Appearing in the record, the reasons assigned by the Commission for its action in this respect are that there was good reason to believe that the rates being exacted were excessive; that an unjust exaction was being demanded from the gas users; that the case had been pending for three years and that it was to the benefit and interest of all that the matter be speedily adjudicated. These are cogent reasons supporting the action of the Commission under a statute vesting it with authority to dispense with the intermediate report in a case such as this.

Colorado, however, strenuously contends that there are present facts which stamp the action of the Commission as arbitrary and that by such action it was denied that due process to which it was entitled as a matter of law. It contends that the proceeding was adversary and accusatory in nature; that the issues of fact were sharply drawn and that there was conflict in the basic facts as well as an issue of the credibility of the witnesses; that the trial examiner who heard and saw the witnesses was best able to appraise and resolve this conflict in the evidence and, having seen the witnesses in the first instance, pass on their credibility, and that therefore dispensing with the examiner's report deprived it of his observations with respect to these matters, which he alone could make.

For support of this contention, Colorado relies in large part on what was said by the Supreme Court in *Universal Camera Corporation* v. *National Labor Relations Board*, 340 U. S. 474. That case involved a charge of unfair labor practices under the Labor Act. The board rejected the examiner's findings and did not take them into consideration in its consideration of the case. This the Supreme Court said was error. But all the court held was that the trial examiner's report constituted evidence which should be considered along with all other facts and circumstances by the board in reaching its conclusion whether there was substantial evidence showing a violation. There was not involved the question under what conditions, if any, the examiner's report might be dispensed

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where cases present sharply contested issues of fact, agencies should not as a matter of good practice take advantage of the exemptions." Senate Docket No. 248, 79th Congress, Second Session, Page 216.

"There are, however, some instances of either kind of case (rule making and licensing) which tend to be accusatory in form and involve sharply controverted factual issues." Senate Docket No. 248, 79th Congress, Second Session, Page 262.

"* * * if issues of fact are sharply controverted, or the case or class of cases tends to become accusatory in nature * * *." Senate Docket No. 248, 79th Congress, Second Session, Page 273.

Like and similar statements appear in the reports of the Committees.

with. It is obvious that the issues arising in a labor board case, charging unfair labor practices, differ materially from those arising in a rate hearing case before the Federal Power Commission, such as we have here. In a labor board case the facts are always in sharp conflict and the credibility of witnesses many times involved.

To set out in detail the evidence which in our opinion warrants the conclusion that there was no disputed issue of fact would extend this opinion, which of necessity must be lengthy, to undue length. We, therefore, content ourselves with saying that a careful analysis of the record does not in our view sustain the contention that there was any material conflict in the basic facts or that the credibility of witnesses was an issue. The facts with respect to the financial structure of Colorado, its gross revenues, as well as its expenditures, were all taken from the company's books. With slight variation the facts as revealed by Colorado's books were taken as the basic facts considered by the Commission in reaching its conclusions. The line of cleavage came with respect to the methods to be employed in allocating revenue and expenditures between jurisdictional and non-jurisdictional operations and the proper method by which to fix depletion, as well as other relevant matters. The difference between the parties involved difference of opinion and the inferences and deductions to be drawn from established basic facts. These issues arose in specialized fields calling for the opinion of experts. It was not a question of the credibility of the expert witnesses but rather a question of the weight to be accorded to their opinions. The Commission was as competent to pass on these questions without the examiner's intermediate report as with it because these questions were plainly within the Commission's expert competency.[4]

Colorado makes the further contention that the proceedings are fatally defective because it was not given the notice required by 5 U.S.C.A. § 1003 (a). Its contention in this respect is that it was not notified or advised of the contention of the Commissioner's Staff. It points to the fact that the Staff introduced three cost of service studies relating to the years 1951, 1952 and 1953 and did not definitely state which one it stood on until after the hearings were closed.

But the notice to which Colorado was entitled prior to trial under Section 1003 (a) was not of the position the Staff (the prosecuting agency) would take at the hearing. Under Section 1003 (a) it was entitled to notice of "a description of the subjects and issues involved" in the proceeding and such notice it had. There was never any doubt as to the issues and matters involved in the hearing. Colorado, like the Staff, likewise introduced three alternative cost

[4] *Gloyd* v. *Commissioner of Internal Revenue*, 63 F. (2d) 649, and cases there cited.

of service studies during the hearing. It is without dispute that Colorado's operations in 1952 were taken as the test period and that Colorado at all times knew of the contentions made with respect to such operations and had ample opportunity to meet them and prepare its case.

Jurisdiction of the Commission and Scope of the Review

Before going to a consideration of the substantive issues raised by Colorado, it might be well to set out the basic principles of law delineating the Commission's jurisdiction and our scope of review. The primary purpose of the Natural Gas Act was to protect the users of gas against exorbitant exactions at the hands of the natural gas companies and on the other hand assure to them the right of a fair return from their operations.[5] The duty and jurisdiction to effectuate these broad principles were lodged with the Commission. The Act provides that all rates shall be just and reasonable. It not only empowers but makes it the duty of the Commission, when necessary, to hold hearings to determine just and reasonable rates and fix the same by order. Any aggrieved party may petition the appropriate circuit court of appeals for review. Such court is vested with exclusive jurisdiction to affirm, modfy, or set aside in whole or in part such order. But our scope of review is a limited one. The Act provides that "The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive."[6] In the Jersey City case, cited in Footnote 6, the Supreme Court quoted with approval from the Hope case, as follows: " 'Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences.' " It is in the light of these principles that we examine the entire record to determine whether the Commission's findings are supported by substantial evidence. If they are, we may not set them aside merely because we, as the triers of the facts, might reach different conclu-

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[5] *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591.

[6] Section 19 (b); see also *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591; *I. C. C.* v. *Jersey City*, 322 U. S. 503; *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 142 F. (2d) 943; *Cities Service Gas Co.* v. *Federal Power Commission*, 155 F. (2d) 694.

sions. We will consider the assignments of error in the order set forth in Colorado's brief. They are as follows:

The Commission Failed to Make Adequate Findings Between Jurisdictional and Non-Jurisdictional Sales

Under this heading Colorado contends that the Commission did not show an allocation of cost of service among petitioner's several classes of customers and did not make findings as to the determinants necessary for it to verify that it will be able to earn under the several rate schedules prescribed by the Commission the fair return allocated by the Commission. In the first place, Colorado does not contend that there is no evidence in the record that it will be able to earn the sum of $10,289,269 under the new rates fixed by the Commission. Table II of the Commission's opinion does show the allocation of the total cost of service broken down as to well mouth, gathering and products extraction, with respect to direct sales, total transmission, systems, leased transmission facilities and other operations. Tables III, IV and V of the opinion show additional details as to such allocations. In the absence of any claim or showing that the revenues found by the Commission under its allocations will not accrue, Colorado may not complain because the cost of service is not further broken down.

Not much need be said with respect to the contention that no findings were made with respect to the determinants necessary for Colorado to verify that it will be able to earn under the several rate schedules the return allowed by the Commission. It seems to be conceded that both parties used billing demand and commodity value as determinants and that they were also used by the Commission. By the application of these two determinants to the rate schedules, the rate of return can be ascertained. It was, therefore, not necessary for the Commission to make specific findings with respect to these determinants, which admittedly were used by it as well as the parties to the litigation.

The substantive issues in conflict center around three items which must be considered in determining total cost of service. While the cost of service found by the Commission was $3,484,784 less than that found by Colorado, it challenges only $2,827,778 thereof. To resolve the issues in dispute, it is not necessary to make detailed computations of the items making up this amount. We do not understand that Colorado challenges the correctness of the computations if it be conceded that the treament accorded these items by the Commission is correct. These three items are (a) loss, if any, from gasoline extraction, (b) percentage depletion allowance, and (c) fair rate of return.

Gasoline Operations

Prior to this proceeding, Colorado sought and obtained permission to merge the properties of Canadian River Gas Company. Under the merger it was proposed to transfer from Canadian River to Southwestern Development Company, or its nominee, the liquid hydro-carbons in the gas production by Canadian River from the West Panhandle Field. Colorado was to continue to process the wet gas to remove the liquid hydro-carbons. Under this arrangement the revenues derived by Canadian River from the extraction and sale of natural gasoline, which had theretofore been used to reduce the cost of gas purchased by Colorado from Canadian River,[7] would be lost upon the consummation of the merger. The authorization for the merger was granted upon the express condition that whereas rights to liquid hydro-carbons in place were granted to the Southwestern Development Company and whereas Colorado was to receive 50% of the gross proceeds from the sale of certain liquid hydro-carbons and 15% of the net revenue was to be received by Colorado from the hydro-carbons resulting from the operation of Fritch Natural Gas Plant of Texoma Natural Gas Company, that if the cost properly allocable to such hydro-carbons exceeded the amounts payable to Colorado pursuant to such transactions then and in that case *in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess should not be considered as a cost of service to Colorado's natural gas customers and consumers.* The Commission determined that there was a loss from such operations and deducted the amount it found as the loss from the cost of service. Colorado on the other hand contends that there was a net profit from such operations. Whether there was a loss depends upon whether the methods of allocation of certain costs of operation adopted by the Commission were proper.

All parties recognized that since the liquid hydro-carbons are contained in the wet gas stream the cost of producing and gathering such wet stream to the inlet of the gasoline plants is a joint cost which must be allocated upon some reasonable basis between dry gas and gasoline. The Staff's method of relative market value was adopted by the Commission as a proper method of allocation. Under this method the joint costs were apportioned to the dry gas and gasoline on the basis of the relative market value of the finished products. The direct costs to make each product fully marketable was deducted from the respective market values of the finished prod-

[7] See *Colorado Interstate Gas Company* v. *Federal Power Commission*, 324 U. S. 581.

ucts, so as to determine relative market values at the point of processing, where operations cease.

For the respective market value the Staff recommended and the Commission used 5 cents per Mcf as the value of dry gas, and as the value of gasoline the total gasoline revenue for 1952, as estimated by Colorado, less the direct cost to make the gasoline marketable, and other direct gasoline costs. The treatment to be accorded the costs within the plants will be discussed later in the opinion. Colorado on the other hand allocated the well mouth and gathering cost on what is termed a volumetric method, based on the shrinkage of the wet gas volume while being processed.

Colorado's contention that the Commission did not approve the relative value method as a proper method of allocation finds no support in the record. True, it did say that neither method was entirely satisfactory, but the same could be said with respect to any method which might be proposed. Mathematical exactness in the apportionment of cost is an impossibility. Because a method may have some infirmities does not of itself condemn it as a proper method.[8] It is the duty of the Commission to select that method which in its considered judgment more nearly reaches a just and sound result. The Commission did approve and apply the relative value method, and without extended discussion, we think its conclusion with respect thereto finds support in the record and is, therefore, approved.

Colorado's contention that there is no evidence in the record supporting the Commission's valuation of 5 cents per Mcf for dry gas and, if that method were to be employed, that 10 cents should have been fixed as its value, is without merit. Without setting out the evidence in detail, it is sufficient to say that the evidence on which the Commissior relied in fixing the value at 5 cents is a least as convincing, and perhaps more so, than the merger testimony of one witness on which Colorado relies to fix the value at 10 cents.

The more difficult question is whether the Commission correctly eliminated the loss from these gasoline operations from the cost of service. The gasoline operations were as much a part of Colorado's business as any other operation. Save for the provision in the merger order hereinbefore italicized, the total costs of the operation of this department would have of necessity been considered as a part of the total cost of service. The Commission seeks to justify its elimination of the loss from the cost of service under the provision in the merger order that such loss should not be taken into account in establishing new rates.

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[8] *Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U. S. 581.

Throughout all the decisions runs the basic principle that the important and deciding factor in rate hearings is the end result. They emphasize that a reviewing court is more concerned with the end result than with the multiple detailed mechanics employed in reaching it. This was emphasized by us in *Colorado Interstate Gas Company* v. *Federal Power Commission*, 142 F. (2d) 943, and in *Colorado Interstate Gas Company* v. *Commission*, 324 U. S. 581, 603, where the Supreme Court again stated, "It is not the theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry * * * is at an end." Conversely, if the total overall effect of the rate order is to deprive the utility of the opportunity to earn a fair return, it cannot stand.

It would seem that the elimination of the loss of the gasoline operations from the cost of service deprives Colorado of earning the fair rate of return to which it is entitled. It means that this loss must come out of the net profits of the stockholders notwithstanding that it is an element of cost of service. Nor is it an answer to say that this was a condition of the merger order and that, therefore, Colorado's stockholders are bound and saddled with this loss. We are dealing here with a business affected with a public interest. Parties in such businesses are not free to contract as they choose. They are subject to regulation by proper Governmental authority. In the exercise of its jurisdiction, such authority must be fair, both to the public and to the utility. It is the statutory duty of the Commission to establish on the one hand rates that are fair and just to the utility and on the other hand to strike down rates that demand an unlawful and unreasonable exaction. A rate based upon the exclusion from the cost of service, no matter for what reason, of a subsantial amount of admitted operative cost does not and cannot reach a just end result and may, therefore, not stand.

The provision in the merger order that such operative costs as we are considering here should be eliminated from the cost of service base in subsequent rate hearings does not alter these basic principles. When that proceeding was before the Commission, it was its statutory duty to determine whether the plan was fair and just to Colorado's gas users. If it found that it might result in an unjust burden on them, it had power to disapprove it. It could not predicate its approval thereof upon a condition which it could not adopt in a rate hearing and which would thereafter deprive Colorado of the opportunity to earn a fair return upon its investment.

Costs Within the Gasoline Plants

The Commission did not adopt in whole the method championed either by its Staff or Colorado for allocating costs within the gasoline

plants. In some respects it agreed with Colorado's contentions and made an allocation based thereon. In others it adopted a method proposed by its Staff. Since no issue is raised in the petition for review with respect to these allocations, we do not deem it necessary to further notice or discuss this element of allocation of joint costs.

Percentage Depletion

Under the Tax Code, a producer of natural gas is allowed an annual deduction for depletion of 27½% of the well head value of the gas, not to exceed 50% of the net income. The treatment of this item is one of the major points of conflict in this case. It is, of course, obvious that the greater the amount of deduction for depletion the less remains of income in which to pay an income tax and correspondingly less will be the amount of the income tax which may then be included as an element of cost of service. The Commission fixed the value of the well head gas for this purpose at five cents per Mcf and then used that sum in determining the depletion allowance to be deducted from gross income for the purpose of computing income taxes. The income taxes so computed were then included as an element of the total cost of service. Colorado contends that the only proper value for this purpose was 3.17 cents. It asserts that the erroneous use of 5 cents per Mcf had the effect of increasing Colorado's percentage depletion deduction for federal income tax purposes by $938,449, which in turn had the effect of reducing the allowance of federal income taxes as an element of cost of service by $1,016,653.

Colorado's contention that the 3.17 cents is the only correct value which may be fixed on the gas at the well head is based on the fact that in 1946 the Bureau of Internal Revenue fixed this value on the gas for income tax computation purposes for Canadian River and that it has been thus used ever since. It argues with some force that if it is required to compute percentage depletion on a 5 cents valuation for rate fixing purposes and thus received a lower rate because of a greater depletion from the cost of service based and, when it then later files its income tax return is permitted to deduct depletion allowances on a value of only 3.17 cents, its actual income taxes will be measurably higher than those computed in determining its rate base and that thus the rate so fixed will result in an unfair rate of return.

The Commission contends that Colorado is estopped to deny that 5 cents is the proper value to place on the well head gas by reason of the fact that its application to the Commission for authority to merge with Canadian River it represented that a saving would be effected in Federal income taxes by the fact that Colorado's

depletion allowance would be based on a 5 cents value instead of 3.17 cents and that this representation was accepted by the Commission and was a factor inducing it to grant the merger order. Since we do not rest our decision on estoppel, it is not necessary to resolve this question.

We have already said there was substantial evidence supporting the Commission's finding of a 5 cent well head gas value. The question then is should it have surrendered its considered judgment with respect to this value and have adopted a value of 3.17 cents, because that was the valve fixed in 1946 by the Internal Revenue Department for depletion allowances for Canadian River. To do so would in our opinion constitute an abdication and surrender of a duty placed upon the Commission by the Act. It could discharge its functions of ascertaining a fair rate of return only by considering all relevant factors necessary for such a determination as of the time of the inquiry. This it is obvious included the present value of the well head gas for depletion purposes. In fixing this value, it was required to exercise its own judgment rather than fix a value merely because it had been adopted by another agency for another purpose and at another time.

Government is carried on through many more or less independent, although correlated, agencies which must work together toward a common objective. It can function efficiently and without injury to its citizens in many instances only if there is proper cooperation and recognition of interdependent relations between these various departments. It is not to be assumed in advance that the Internal Revenue Department will disregard a finding by the Commission in this respect without good cause and will arbitrarily adhere to a fixed depletion value for gas, adopted six years before, which will work serious injury to Colorado but, if so, and as pointed out by the Commission, it would then become a matter for future consideration. It is no reason to ask the Commission to not discharge its duty in finding the fair present marketable value of the gas in question.

Rate of Return

Colorado contended for a 6½% rate of return. The Commission fixed 5¾% as a fair rate of return. It found that such a rate of return would produce a return for the common stock equity of Colorado of 8.45%, after allowing ½% for cost of financing, after servicing of Colorado's debt and preferred stock requirements and after allowing for all income taxes. From this the Commission concluded that such rate of return was wholly adequate to insure confidence in the financial soundness of the utility to maintain its credit and to enable it to attract capital necessary for the proper

discharge of its public duties. The capital structure of Colorado considered by the Commission is set out in its opinion as follows:

		Amount	Percent
"Long-term Debt		$29,600,000	53.9%
Preferred Stock		2,000,000	3.6%
Common Equity			
Common Stock (1,711,016.6 shares)	$ 8,555,000		
Surplus	14,759,000		
		$23,314,000	42.5%
		$54,914,000	100.0%

The outstanding long-term debt of Colorado consists of four issues of long-term serial notes as follows:

2% Notes, due $400,000 semi-annually May 1, 1952 through May 1, 1954	$1,200,000[14]
2¾% Notes, due $400,000 semi-annually November 1, 1954 through November 1, 1964	8,400,000
3⅛% Notes, due $250,000 semi-annually October 1, 1952 through April 1, 1969	8,000,000
3¾% Notes, due $400,000 semi-annually February 1, 1955 through August 1, 1969	12,000,000

[14] Excludes $800,000 of such notes due within one year included in current liabilities."

From this the Commission found that the weighted average cost of the debt was 3.25% for all of its outstanding long-term debt; that the preferred stock bore a dividend rate of 6%.[9] The Commission noted that the most recent issue of notes sold by the company bore a rate of 3¾% interest which rate exceeded the average rate on all the outstanding long term debt. Considering Colorado's contention that this indicated that future interest charges would exceed the weighted average cost of the entire outstanding debt, the Commission said, "But Colorado's contention presupposes that rate making is not a continuing process and that appropriate adjustments of rates cannot be made when experience demonstrates that adjustment is required. We find that the actual cost of the company's outstanding long-term debt and preferred stock is a proper measure of the cost of borrowed money and of preferred stock funds in determining a fair rate of return for Colorado in this case."

[9] Colorado had stated to the Securities and Exchange Commission that this debt would be retired on or before December 31, 1952.

While the Commission in its opinion states that there was "in this record an abundance of evidence on the subject of rate of return including average yields for bonds of public utilities, railroads and industrials as well as U. S. Treasury bonds; data on public offerings of natural gas bonds, preferred and common stocks; earnings-price ratios of various natural gas companies' common stocks; natural gas companies' capitalization ratios and data as to Colorado's outstanding securities, its earnings and financial requirements.", it is clear to us that no consideration was given by the Commission to factors other than the financial history of nine natural gas companies subject to the Commission's jurisdiction, whose common stock was held by the public, and seven natural gas companies, whose common stock was traded on recognized exchanges, and the data with respect to Colorado's outstanding securities, its earnings and financial requirements.

From an objective study of the investor's appraisal of the common stock of nine natural gas companies held by the public during the five year period ending August, 1951, the Commission found that investors had required a return on the average on the issues sold to the public of 8.3%. Colorado calls attention to the fact that the exhibit reflecting this study does not contain the names of these companies nor does their name appear in the record. They are, however, the nine gas companies reporting to the Federal Power Commission and it is not contended the information reflected in the exhibit is not correct or that Colorado did not in fact know or could not ascertain which companies were included in the study. The Commission further found that the average earnings price ratio of the outstanding common stock of seven natural gas companies traded on recognized exchanges for the same period to be 8.2%, with the average for the last twelve months of the period of 7.5% and decreasing to 6.4% as of October, 1951, and that at the latest date shown by the record, July, 1951, the yield varied from 3.5% to 6.4%. The Commission also found persuasive evidence as to the cost of equity capital in the experience of Colorado itself. It alluded to the fact that two principal stockholder groups had offered 966,000 shares of its common stock for sale to the public; that this was the first public offering ever made of Colorado's common stock and represented 56% of the total stock; that the book value of the stock was $13.63 per share; that it was offered at $26.75 to net the selling stockholders $25.25 per share; that based on earnings for 1951 of $1.88 per share the earnings—offering price ratio was 7.03%, and the earnings—net price to the selling stockholders was 7.44%; that the public offering of this stock was oversold. Whether the

While it is true that the Commission allowed as an item of cost of service only the weighted average cost of Colorado's outstanding debt of 3.21% and allowed nothing additional because the most recent borrowing reflected a higher interest rate of 3.75%, we do not think this constitutes basic error. The 3.75% issue was included in reaching the weighted average of 3.21%. Sufficient was allowed as a cost of service to retire the entire outstanding debt. Of course, if there was evidence establishing an upward trend in interest rates, it should have been taken into consideration but apparently this one borrowing is all of which there is evidence in the record and of itself is not sufficient to establish a reasonable expectation of a future upward trend. We are of the further view that the record amply supports the Commission's finding that Colorado has no plans for and does not presently contemplate a refinancing program in the near foreseeable future. Under these circumstances, the Commission did not err in refusing to give consideration to the higher interest rate in this one note issue.

While as pointed out in *Power Commission* v. *Hope Gas Company*, 320 U. S. 591, and related cases, there is no single formula or combination of formulae which may or can be used in determining rates, and as further pointed out, pragmatic adjustments are of necessity involved in rate making procedure, there is a well settled basic principle concerning which there can be no dispute. The rate must be fair and reasonable and, as pointed out in the Hope case, such a rate is one that will produce enough revenue to pay operating expenses, provide for the capital costs of the business, and for a return to the equity owners "commensurate with returns on investments in other enterprises having corresponding risks." As stated by the Supreme Court in the Hope case, "By that standard the return to the equity owners should be commensurate with returns on investments in other enterprises having corresponding risk." The court there approved the method employed by the Commission in reaching its conclusion. It pointed out that the Commission had "considered the financial history of Hope and a vast array of data bearing on the natural gas industry, related businesses, and general economic conditions."

It would seem that the history and experience of other successful companies engaged in the production, transportation and sale of gas would furnish the best guide as to what was fair and adequate. True, there are many companies engaged in the production and transportation of natural gas which apparently were not considered. Most of these are not subject to the Commission's jurisdiction, no doubt because they are local in their operations and not engaged

and to all such companies whose common stock was traded on recognized exchanges, as well as to Colorado's outstanding securities, its earnings and financial requirements. It also attached significance to Colorado's experience in the public offering for sale of 56% of its common stock. The fact that this offering was promptly oversubscribed is evidence of the standing of Colorado with the investing public and, if we must as urged by Colorado take into account that the eagerness to purchase this stock was induced in the belief of the future development of Colorado's resources, we must on the other hand not be unmindful that that manifested interest was in the fact of a rate hearing which might well, as it did, result in a decrease of rates.

We believe that the experience of other comparable gas utility companies, having a sound financial structure and long experience of successful operation, is a better criteria by which to gauge and determine the adequacy and fairness of rate of return than that of railroads, power transmission companies or other like utilities engaged in other fields and under other conditions and circumstances, or the rate of return on Government bonds or industrial bonds in unrelated enterprises. We do not say that such factors are not proper for consideration but on the other hand failure to give them weighty consideration does not in our opinion constitute reversible error on the record before us in light of the factors that were considered in this case.

While the rate of return of 5¾% is lower than any rate heretofore established which has been called to our attention, that in itself is not suspect nor may we overturn it merely because we as the trier of the facts might have established a higher rate. From the record we cannot say that a rate of return of 5¾% properly computed is unreasonable and therefore confiscatory.

The late case of *State Corporation Commission of the State of Kansas* v. *Federal Power Commission*, decided by the Eighth Circuit on July 20, 1953, in which the findings and order of the Commission were reversed and remanded in part for further consideration with respect to making additional findings, has been called to our attention. It is sufficient to say that in our opinion the two cases are distinguishable and that the facts in this case do not warrant similar treatment other than above indicated.

Summarizing, it is our conclusion that the Commission's findings and order based thereon are supported by the record save only with respect to its findings relating to the loss from the gasoline operations. The disapproval of its treatment of this item makes neces-

In all other respects save this the findings and determinations by the Commission are approved.

The order of the Commission is, therefore, REVERSED and the cause is REMANDED for further proceedings in accordance with the views expressed in this opinion.

NUMBER 4541

BRATTON, Circuit Judge, concurring.

I concur in the reversal of the order of the Commission. But I think the reversal should also rest upon the additional ground that the action of the Commission in omitting the intermediate decision procedure constituted error. Where an examiner is named in a proceeding of this kind and he conducts the hearing, the intermediate decision procedure is the general rule; and its omission is the exception. The omission of the intermediate decision procedure is warranted only where the Commission makes a well founded and sustainable finding that due and timely execution of the functions of the Commission imperatively and unavoidably so requires. 5 U. S. C. A. § 1007(a).

The Commission found that due and timely execution of its functions imperatively and unavoidably required it to omit the intermediate decision procedure in this proceeding. But that primary finding was predicated upon two subsidiary findings. One of such subsidiary findings was that the proceeding had been in progress for a regrettably long period of time. But the Commission expressly stated in connection with such finding that the long delay was not attributable to any one particular party. And the other subsidiary finding was that in view of the fact that the Commission had no power of reparation with respect to past rates, which might or might not prove to be excessive, it appeared that the record in the proceeding presented the kind of situation requiring the omission of the intermediate decision procedure as provided in the Administrative Procedure Act. But in every proceeding of this kind the Commission does not have the power of reparation in respect to past rates which are found to be excessive. Virtually all of the testimony was given by expert witnesses. But their credibility and the weight to be given to their testimony were matters for consideration in resolving conflicts in the testimony respecting basic facts upon which the outcome of the proceeding depended at least in part. The examiner saw the witnesses and observed their demeanor while testifying. He was in the best position to determine their credibility and weigh their testimony. There

omission of the intermediate decision procedure. And in the circumstances, the omission of such procedure was prejudicial error.

JUDGMENT

Twenty-Ninth Day, September Term, Thursday, October 29, 1953. Before Honorable Sam G. Bratton. Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard on the transcript of the record from the Federal Power Commission and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the order of the Federal Power Commission in this cause be and the same is hereby reversed, and that this cause be and the same is hereby remanded to the said Federal Power Commission for further proceedings in accordance with the views expressed in the opinion of the court.

Filed. United States Court of Appeals Tenth Circuit. Nov. 25, 1953. ROBERT B. CARTWRIGHT, *Clerk*.

UNITED STATES COURT OF APPEALS TENTH CIRCUIT

No. 4541

COLORADO INTERSTATE GAS COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

AND

CITY AND COUNTY OF DENVER, AND PUBLIC UTILITIES COMMISSION OF COLORADO, INTERVENORS

PETITION FOR REHEARING OF FEDERAL POWER COMMISSION, RESPONDENT

The Federal Power Commission, Respondent, respectfully petitions this Court for rehearing of that part of the Court's opinion and judgment entered pursuant thereto filed October 29, 1953, holding that the Commission's exclusion from the cost of service of the loss on gasoline operations was improper notwithstanding the condition of the merger order that such loss was not to be considered as part of the cost of service to be borne by the consumers in any Commission rate proceeding. The Court said (typewritten

operative cost does not and cannot reach a just end result and may, therefore, not stand.

Grounds for Rehearing

The Federal Power Commission seeks rehearing on the following grounds:

1. The Court could not consider the validity of the condition of the merger order providing for the exclusion of any loss on gasoline operations from the cost of service and the exclusion of the loss pursuant to that condition, since objection to such exclusion had not been raised by Petitioner as required by Section 19 (b) of the Natural Gas Act.

2. The validity of the merger condition providing for the exclusion of any loss on gasoline operations and the exclusion of the loss pursuant thereto were not open to collateral attack or to review under the "end result" test as assumed by the Court.

3. Assuming, *arguendo*, that the basis for the exclusion of the loss on gasoline operations was before the Court under the "end result" test, the Court erred in holding that the "end result" of the Commission's rate order was unjust and unreasonable.

Argument

Before discussing the three grounds set forth above, the Commission respectfully submits that a petition for rehearing is particularly appropriate in this instance because the matter decided adversely to the Commission by the Court was raised by the Court on its own motion. No objection to the exclusion of the loss on gasoline operations from cost of service was raised by Petitioner at any time before the Commission during the administrative rate proceedings or before the Court. Accordingly, the issue was never briefed or argued by any party to the proceeding and was not the subject of inquiry at the oral argument on the part of the Court.

1. *This Court could not, sua sponte, consider the propriety of the exclusion of the loss on gasoline operations from cost of service.* Section 19 (b) of the Natural Gas Act (Act), (52 Stat. 831; 15 U. S. C. 717r (b)), under which the present review proceedings were instituted by Petitioner and which is the sole basis for this Court's jurisdiction provides, in pertinent part, as follows:

> * * * No objection to the order of the Commission shall be

There is no question that Petitioner did not object to the condition of the merger order in this case or to the exclusion from the cost of service of the loss, if any, on gasoline operations. Indeed, Respondent stated, without challenge, to this Court, at page 34 of its brief:

> * * * With respect to the computation of the loss on gasoline operations, Petitioner does not challenge the propriety of such deduction if there is a loss on the gasoline operations. (See also: Resp. Br. pp. 54, 55; Pet. Br. p. 29, Eighth Point).[1]

Petitioner objected only to the method of allocation employed by the Commission in determining that there was a loss on the gasoline operations. The Court overruled Petitioner's objections in this respect and, having done so, we respectfully submit that review was at an end so far as the loss on gasoline operations enters into review of the rate order. For the prohibition of Section 19 (b), quoted above, which bars a petitioner from urging an objection in the court not previously raised on application for rehearing before the Commission, also bars consideration of the objection by the Court at the behest of petitioner or on the Court's own motion. In fact, the prohibition of Section 19 (b) is directed to the Court: "No objection * * * shall be considered by the court * * *."

The use of the word "shall" negates any concept of a discretionary power in the Court, on its own motion, to consider an objection not previously raised by the Petitioner. And this is the case even though Section 19 (b) further provides that an objection raised by a petitioner for the first time on review may be considered by a court if there was "reasonable ground for failure so to do." *Section 19 (b)*. Here no finding of "reasonable ground for failure so to do" was made or could be made by the Court. Petitioner accepted the validity of the merger condition and the treatment of the loss on the gasoline operations pursuant thereto.

In these circumstances, the Court had no power to pass on the issue. *Panhandle Eastern Pipe Line Company* v. *Federal Power Commission*, 324 U. S. 635, 649 (1945); concurring opinion, pp. 650-651; *American Power & Light Company* v. *Securities and Exchange Commission*, 146 F. 2d 606, 612-613 (C. A. 1, 1944) *affirmed*, 329

[1] Pursuant to the stipulation of all parties and approved by the Court, page references herein to the record are to the pages of the record as certified by the Secretary of the Commission to this Court. Citations to the record will be referred to in this petition as "R." followed by the page number. References to Petitioner's Brief to this Court will be referred to as "Pet. Br.", and references to Re-

U. S. 90 (1946); *National Labor Relations Board* v. *Cheney Calif. Lumber Co.*, 327 U. S. 385 (1946); *United States* v. *Hancock Truck Lines, Inc.*, 324 U. S. 774 (1945); *Unemployment Compensation Commission of Alaska* v. *Aragon*, 329 U. S. 143, 155 (1946).

In the *Panhandle* case, *supra*, the natural-gas company's failure to raise the objection in an application for rehearing before the Commission was held to preclude court review under Section 19 (b), absent a showing of "reasonable ground for failure so to do." The Supreme Court did not consider that the issue nevertheless remained open on its own motion.

The Supreme Court's decision in the *Cheney* case, *supra*, expressly denies authority to consider an issue not raised by the parties. In that case the lower court struck out a paragraph of a Labor Board order to which the company had raised no objection when the proceeding was before the Labor Board. Although the review provisions of the National Labor Relations Act are similar in intent to those involved here, the Labor Board interposed no objection to the lower court's action and made no claim that the failure to make timely objection to the Labor Board barred court consideration of the issue. Notwithstanding this, the Supreme Court raised the point itself, because the failure to make timely objection was basic to the court's jurisdiction to review and therefore "decisive" of the case, saying that the review provisions were a "limitation which Congress has placed upon the power of courts to review orders of the Labor Board" (327 U. S. at 388).

So, also, in the *Hancock* case, *supra*, "despite the fact that, neither on brief nor in oral argument, did the appellants' counsel press for reversal on" the ground that appellee had not objected to the matter on which the lower court's action had been based, the Supreme Court said (324 U. S. at 779):

> * * * we think the district court committed reversible error, *of which we must take note*, in passing on the merits of the case made by the appellee [emphasis supplied].

It "was manifestly improper," the Court held (324 U. S. at 779-780), "to reverse the Commission's order in respect of a provision therein as to which the suitor had advised that body it no longer objected but acquiesced."

These cases emphasize the fact that the objection we raise under this point is not a technical one. They show that the objection is so fundamental that the courts have, *sua sponte*, noticed the prohibition on their jurisdiction to review an issue where the prerequisites for review have not been met.

the Supreme Court said in the *Aragon* case, *supra* (329 U. S. at 154-155):

> Nor can we accept the arguments of the majority of the Court of Appeals that since negotiations between the companies and the workers were carried on in San Francisco and Seattle, the dispute could not be said to be "at" the Alaskan establishments as required by the statute. So far as we are able to determine, this issue was injected for the first time by the opinion of the majority of the Court of Appeals. The contention does not seem to have been raised or pressed by respondents up to that point. The responsibility of applying the statutory provisions to the facts of the particular case was given in the first instance to the Commission. A reviewing court usurps the agency's function when it sets aside the administrative determination upon a ground not theretofore presented and deprives the Commission of an opportunity to consider the matter, make its ruling, and state the reasons for its action.

2. *The Court's reversal constitutes a collateral attack and review of the merger condition, since neither the merger condition nor the treatment of the loss on gasoline operations was before the Court under the "end result" test.* Petitioner had ample opportunity to secure judicial review of the order authorizing the merger including the conditions thereto attached. Having failed to seek judicial review of that order, Petitioner itself could not collaterally attack the merger order in this proceeding, particularly where, as here, it was and is retaining the benefits of the merger. Where there is an exclusive statutory provision for direct review, representing "a distinctive formulation of the conditions under which resort to the courts may be made" (*F. P. C.* v. *Pacific P. & L. Co.*, 307 U. S. 156, 159 (1939)),[2] court decisions have made it abundantly plain that collateral review will not be permitted not only of questions as to the merits of the order (*Louisville Gas & Electric Co.* v. *F. P. C.*, 129 F. 2d 126 (C. A. 6, 1952); *Woods* v. *Kaye*, 175 F. 2d 886 (C. A. 9, 1949); *Miles Laboratories* v. *F. T. C.*, 140 F. 2d 683, 684 (C. A. D. C., 1944), *certiorari denied*, 322 U. S. 752 (1944)), but of constitutional questions (*Yakus* v. *United States*, 321 U. S. 414 (1944); *United States* v. *Ruzicka*, 329 U. S. 287 (1946); *LaVerne Co-op. Citrus Ass'n.* v. *United States*, 143 F. 2d 415 (C. A. 9, 1944)), and of questions of the administrative agency's jurisdiction (*Lichter* v. *United States*, 334 U. S. 742 (1948); *Piuma* v. *United States*, 126

[2] The Supreme Court was there speaking of Section 313 (b) of the Federal Power Act which is the same as Section 19 (b) of the

F. 2d 601 (C. A. 9, 1942), *certiorari denied*, 317 U. S. 637 (1942)). See also: *Ewen* v. *Peoria & E. Railway Co.*, 78 F. Supp. 312, 332-333 (D. C. N. Y., 1948), *certiorari denied*, 336 U. S. 919; *United States* v. *Railway Express Agency*, 101 F. Supp. 1008, 1012 (D. C. Del., 1951). By parity of reasoning, the order and conditions therein were also immune from attack and collateral review by the Court.

The force of this argument, and of those presented under point 1, above, is not dissipated by the proposition that the test of a rate order when challenged is its "end result." In the first place, this Court could not conclude that the "end result" is unjust and unreasonable without rejecting the basis for the disallowance—namely, the merger order condition (typewritten opinion, pp. 20-22). So that even under the "end result" test as applied by this Court the conclusion is inescapable that this Court collaterally reviewed and struck down the provisions of an order not before it and not open to collateral review.[3] In the second place, the "end result" of the rate order is not open to court review unless challenged, and then only to the extent that it has been challenged. Therefore, in *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U. S. 581, 605-606, the Supreme Court said:

> Hence, we cannot say as a matter of law that the Commission erred in including the production properties in the rate base at actual legitimate cost. That could be determined only on consideration of the end result of the rate order, *a question not here under the limited review granted the case.* [Emphasis supplied.]

In the instant case, it is clear that the "end result" of the rate order was not challenged because of the treatment of the loss on gasoline operations. The only "end result" challenge was limited to the proposition that the failure to include gas produced by Colorado in the Panhandle Field at its "value" brings about an unjust and unreasonable "end result" as a matter of law—a contention rejected by the Supreme Court in *Colorado Interestate Gas Co.* v. *Federal Power Commission*, 324 U. S. 581, 605-606 (1945). This Court, therefore, could not because of the "end result" test, *sua sponte*, hold the "end result" unjust and unreasonable because of the

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[3] We draw the Court's attention to the fact that in a direct review of the merger order this Court could only hold that the merger condition was invalid, but could not direct the Commission to approve the merger without the condition. *F. P. C.* v. *Idaho Power Co.*, 344 U. S. 17 (1952). The Commission then would have to determine whether to authorize the merger at all. The result of the

treatment of the loss on gasoline operations and thereby avoid the prohibition of Section 19 (b) and the fact that it collaterally reviewed the merger order.

3. *The Court's reversal of the Commission's disallowance of the loss on gasoline operations is not supported by the "end result" test.* We have argued that the Commission's disallowance of the loss on gasoline operations and the basis therefor were not before the Court in this review proceeding notwithstanding the "end result" test. For purposes of this point, we assume, however, that the disallowance of the loss was open to examination by the Court in this review proceeding by reason of the "end result" test.

On that assumption, we agree that "the important and deciding factor in rate hearings is the end result" and that if "* * * 'the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry * * * is at an end' " (typewritten opinion, pp. 20-21). But the Court erroneously concluded that a "rate based upon the exclusion from the cost of service, no matter for what reason, of a substantial amount of admitted operative cost does not and cannot reach a just end result and may, therefore, not stand."

In reaching this conclusion, the Court has disregarded two important qualifications to the general proposition that from the "investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business." *F. P. C.* v. *Hope Natural Gas Co.*, 320 U. S. 591, 603 (1944). These are (a) that the "rate-making process under the Act, *i. e.*, the fixing of 'just and reasonable' rates, involves a balancing of the investor and the consumer interests," and (b) that there may be conditions under which more or less might be allowed the investor without producing an unjust and unreasonable end result (*Ibid.*).

The record in this case shows that the disallowance of the loss on gasoline operations represents an appropriate "balancing of the investor and consumer interests" and that the disallowance did not impair the investor's confidence in the financial integrity of Colorado.

(a) *Exclusion of the loss on gasoline operations from cost of service represents a proper "balancing of the investor and consumer interests."*

Under the plan for the merger of the properties of Canadian River Gas Company (Canadian River) into Colorado, the liquid hydro-carbons in the gas to be produced by Colorado from the West Panhandle Field were to be transferred to Southwestern Development Company or its nominee. The revenues derived from the sale of natural gasoline were, prior to the merger, applied in

sumers. The record shows (R. 2562) that on Petitioner's own estimate Southwestern's nominee, Westpan Hydrocarbon Company, received $1,428,780 for the test period 1952, and that this entire amount, absent the merger, would redound to the benefit of the rate payers. By the merger, however, more than half of the annual revenues from the sale of natural gasoline was to be diverted to Southwestern's nominee, and Colorado was to be obligated to process the liquid hydro-carbons for Southwestern's nominee. This, it appeared, might require the consumers to bear the full cost of the processing operations without the commensurate benefits of the full revenues derived from such operations.

From the investor point of view, however, advantages appeared to exist in the merger in that, *inter alia*, Colorado would acquire legal title to "very valuable physical assets", the original cost of which, after depreciation, was $10,979,522, and included three trillion cubic feet of natural gas reserves; the corporate structure of the Panhandle-Denver pipeline system would be greatly simplified; and financing of expansions required by Colorado would be facilitated (R. 2738-2740).[4]

Viewing the consumer's interest in the revenues from the gasoline operations and the advantages of the merger from the investor point of view, the Commission found that the merger was in the public interest if the consumers could be protected in some measure against the loss of the benefit of the full revenues derived from the gasoline operations. The Commission thereupon undertook to permit a merger to be effectuated which had advantages while, at the same time, balancing the investor and the consumer interests. The merger condition providing any loss on the gasoline operations should not be considered as a cost of service to be borne by the rate payers was designed to bring about that result and "to avoid any possible doubt as to the full protection to the gas consumers dependent on Colorado" (R. 2740).

Not only was this condition acceptable to Colorado's responsible

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[4] Under a contract between Canadian River and Colorado, Colorado was entitled to receive gas from Canadian River's Panhandle reserves, at cost, so long as there was gas available which Colorado determined as profitable for it to purchase under the cost contract, subject to certain priorities in favor of Texas markets (R. 2727). The bringing of gas to the Denver markets from the Panhandle Field was, in fact, one operation although carried on by two corporations under a "cost" contract whereby Canadian River could not make a profit. Under such an arrangement, however Colorado could not [illegible]

officers and accepted in writing by them (R. 4608), but the condition stems from an undertaking proposed by Colorado's counsel during the course of the merger proceedings before the Commission (R. 2772; see Appendix A to this petition).

While this Court, apparently, views Colorado's assent to the merger on this condition as irrelevant because, the Court asserted (typewritten opinion, p. 21), Colorado is conducting a business affected with a public interest and is not free to contract as it chooses, the Supreme Court in *Interstate Railway Company* v. *Massachusetts*, 207 U. S. 79 (1907), held that the acceptance of a charter subject to a statutory condition to transport school children at half price prevented a public utility from complaining that the condition was unconstitutional on the ground that the public utility was required to transport the school children at less than fair compensation. Cf. *Market Street Ry. Co.* v. *Railroad Commission*, 324 U. S. 548, 562-566 (1945). In any event, as we show hereafter, the "end result" was not unjust and unreasonable.

Not to be overlooked in this connection is the effect of the Court's reversal. Colorado has its merger without the condition and consumers have the loss. In short, the Court's reversal, we submit respectfully, brings about an unjust "end result" and one which is inconsistent with a proper balancing of investor and consumer interests, whereas, as we are about to show, the Commission's balancing of investor and consumer interests does not impair the financial integrity of Colorado.

(b) *The exclusion of the loss on the gasoline operations from cost of service does not produce an unjust and unreasonable "end result."*

The evidence establishes that during the dependency of this rate proceeding before the Commission there was a public offering of Colorado's common stock. There was full disclosure to prospective investors, as appears from the record in this case (R. 2685, 2694), that the pending rate proceeding might involve a rate reduction approximating $3,000,000 and that the earnings available to investors, provided by a Commission rate order growing out of that proceeding, by reason of the condition of the merger, which was fully quoted in the prospectus, would bear the loss on the gasoline operations—that such loss would not be "considered as a cost of service to Colorado's natural-gas consumers" (R. 2685). Notwithstanding all this, the common stock was promptly oversubscribed. As this Court said (typewritten opinion, p. 34):

> The fact that this offering was promptly oversubscribed is evidence of the standing of Colorado with the investing public and, if we must as urged by Colorado take into account that

interest was in the face of a rate hearing which might well, as it did, result in a decrease of rates.

And, it should be added in the face of notice to the investor that the fair return allowed in the rate case would bear the loss on the gasoline operations.

These facts disclose that the investors did not appraise the condition of the merger order respecting treatment of a loss on gasoline operations as liable to impair the financial integrity or credit of Colorado. And that being the case, it cannot be said that the exclusion of the loss on gasoline operations from cost of service brought about an unjust and unreasonable "end result." Thus, while we fully agree that it is the responsibility of a regulatory commission to establish rates that are just and reasonable, the imposition of the condition and the rate order were in full accord with that responsibility.

Therefore, the Court's conclusion that the "end result" of the rate order is unjust and unreasonable is contrary to the evidence.

Conclusion

For each of the reasons assigned, the petition for rehearing should be granted and the opinion and judgment to the extent that the Commission's treatment of the loss on gasoline operations was reversed should be vacated, and the Commission's rate order should be vacated, and the Commission's rate order should be affirmed in all respects.

Respectfully submitted,

Willard W. Gatchell,
General Counsel,
Reuben Goldberg,
Jacob Goldberg,
Attorneys,

Counsel for Respondent Federal Power Commission.

I, Willard W. Gatchell, General Counsel, of the Federal Power Commission and its counsel in this case, do hereby certify that the foregoing petition is presented in good faith and not for purposes of delay.

Willard W. Gatchell,
General Counsel.

November 1953.

APPENDIX A

William A. Dougherty
James Lawrence White

Received Jun 9 1:07 PM '50 Federal Power Commission

Dougherty & White
Room 3020
30 Rockefeller Plaza
New York 20, N. Y.
Columbus 5-5180

JUNE 8, 1950

Hon. Mon C. WALLGREN,
Chairman, Federal Power Commission
Washington 25, D. C.

In re: Colorado Interstate Gas Company, Canadian River Gas Company, FPC Docket No. G-1326

MY DEAR CHAIRMAN: At the oral argument in the above matter the question arose as to whether or not rate payers ultimately receiving gas from Colorado Interstate Gas Company might have to bear an additional cost if at some future time the expense of processing liquid hydrocarbons (mainly, natural gasoline) exceeded the proceeds which Colorado Interstate Gas Company would receive under the plan of merger submitted in the application.

In order to remove this question, I was empowered to state to the Commission that in order to keep a rate payer from meeting this deficiency the Commission could condition the certificate of public convenience and necessity so as in effect to provide that such deficit would not be considered in determining reasonable rates. In other words, the stockholders of Colorado Interstate Gas Company would take the risk as to whether or not gasoline prices will go down. I also stated that we would furnish a proposal to meet the proposition. Accordingly, I submit herewith the type of condition which we believe could be incorporated in this Commission's order and would adequately protect ultimate consumers. Our proposed condition is as follows:

> In as a result of carrying out the terms and conditions of the transactions proposed as a part of the merger of Canadian River into Colorado Interstate whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and thereby Colorado Interstate is relieved [illegible] of the gasoline content from the gas of certain fields [illegible] and [illegible] the net revenue to be received by Colorado Interstate from the operation of the Lucky Natural

Gasoline Plant of Texoma Natural Gas Company, the amounts chargeable as Residuals Operation Expenses (Account 747.2) and Residuals Maintenance Expenses (Account 747.3) exceed the amounts to be paid to Colorado Interstate pursuant to said transaction which is accounted for as Residuals Produced (Account 747.1) and Revenue from Processing Natural Gas (Account 617) then and in that case in any proceeding in which the effective or proposed rates of Colorado Interstate are under inquiry the amount by which said expenses exceed the amount so received and accounted for as Residuals Produced and Revenue from Processing Natural Gas shall not be considered as a cost of service.

Copies of this proposal are being sent to the other Commissioners as well as to Staff Counsel and Counsel for intervenors.

(S.) WM. A. DOUGHERTY

WAD-JHM: dl

ORDER GRANTING PETITION FOR REHEARING OF FEDERAL POWER COMMISSION

Twentieth Day, November Term. Tuesday, December 8, 1953. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard on the petition of the Federal Power Commission for a rehearing.

On consideration whereof, it is now here ordered that said petition for rehearing be and the same is hereby granted, and that the judgment of this court entered on October 29, 1953, be and the same is hereby vacated.

It is further ordered that Colorado Interstate Gas Company file a brief on or before January 4, 1954, responding to the petition for rehearing and brief of the Federal Power Commission.

It is further ordered that this case be set for hearing on January 7, 1954.

ORDER: CAUSE ARGUED AND SUBMITTED ON REHEARING

Thirty-Ninth Day, November Term, Friday, January 8, 1954. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on for rehearing and was argued by counsel. William A. Dougherty, Esquire, appearing for petitioner. I. Goldberg, Esquire, appearing for respondent.

Thereupon this cause was submitted to the court.

Filed United States Court of Appeals Tenth Circuit Nov. 24, 1953 Robert B. Cartwright, Clerk.

UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

No. 4541

COLORADO INTERSTATE GAS COMPANY, PETITIONER,

vs.

FEDERAL POWER COMMISSION, RESPONDENT,

CITY AND COUNTY OF DENVER, and PUBLIC UTILITIES COMMISSION OF COLORADO, INTERVENORS

CROSS-PETITION FOR REHEARING

Colorado Interstate Gas Company, Petitioner in the above entitled matter, being informed that the Federal Power Commission (hereinafter referred to as "Commission") has or will file a petition for rehearing, by its counsel prays that in the event this Court grants the petition for rehearing filed or to be filed by the Commission, that a cross-order be entered to rehear those portions of this Court's decision and opinion set forth in the grounds and reasons given below.

GROUNDS FOR GRANTING REHEARING

Ground One

The Court erred in determining that the omission of the intermediate decision procedure was justified in the circumstances of this case. In determining the intermediate decision issue the Court should recognize that more is required than merely a determination whether discretion has been abused. The Court also should recognize that credibility was involved in this proceeding and that Petitioner and the Court were deprived of an important part of the record.

The substance of the Court's holding on the intermediate decision point is that the Commission may in its sound discretion omit the intermediate decision, and that such exercise of discretion was justified in the case at bar. Also that there were no issues of credibility, but that rather the question was of the weight to be accorded to the opinions of expert witnesses.

A. More Is Required Than Merely A Determination Whether Discretion Has Been Abused

By the Administrative Procedure Act, Congress demonstrated a purpose to impose upon reviewing Courts a responsibility greater than that which had always theretofore been recognized. *Universal Camera Corporation* v. *National Labor Relations Board*, 340 U. S. 474, 490-491, (1951). Even in rule making proceedings, the Administrative Procedure Act does not lodge in an administrative agency an unfettered discretion to omit or not to omit the intermediate decision. Rather such omission shall be made only if there is a finding upon the record that (1) the due and (2) timely execution of the agency's functions (3) imperatively and (4) unavoidably requires the omission. Petitioner does not intend at this stage of the case to reargue all of the requirements and conditions precedent to omission. The Court, however, in deciding that the omission was proper, noted that the reasons assigned by the Commission for its action was that first there was good reason to believe that the rates being collected were excessive; that the case had been pending for three years; and that it was to everyone's benefit that the matter be speedily adjudicated. Petitioner respectfully challenges this sufficiency under the Administrative Procedure Act.

In the first place, the Commission had determined that the lapse of four years between the instigation of the proceeding and the conclusion of hearings was the fault of no one. If it takes such a period of time under administrative processes for a case to go through hearing, that is an inherent difficulty of the process and not one which should add to the authority of the agency to dispense with statutory safeguards. To be rid of harassing delay is never an excuse for avoiding procedural requirements (*Ohio Bell Telephone Co.* v. *Public Utilities Commission*, 301 U. S. 292, 305 (1937); *Inland Steel Co.* v. *National Labor Relations Board*, 109 F. 2d 9, 21 (C. A. 7, 1940)). As a practical matter, an administrative agency which did not wish to observe the ordinary statutory process of an intermediate decision could avoid such process by deliberate delay and then make a finding such as was made in the case at bar and thus lift itself by its own boot straps above a Congressional mandate. Politywise it is a dangerous doctrine which would permit an avoidance or evasion of that which the law would seem to provide.

Secondly, that the Commission believed petitioner's rates were excessive is not a sufficient ground for the omission. A determination of the excessiveness of petitioner's rates was to be a definitive finding made after all procedural safeguards had been observed. For the Commission to assume to make a finding in such respect

and thus avoid its responsibilities in regard to an intermediate decision, would be an arrogance of rights which finds no justification in law, let alone in the Administrative Procedure Act. It cannot be questioned, as this Court has recognized, that the omission of the intermediate decision is to be an exceptional and indeed perhaps a rare thing. There must be elements of evidence aside from the ultimate finding to be made which show imperativeness and unavoidability. Examples of such imperativeness and unavoidability were given at the oral argument in this matter. They, conceivably, could be instances relating to public safety, to war, or possibly to the unavailability of the examiner. The words used by Congress were strong words indeed, and must have been used with a deliberate intent to see that the broad Congressional purpose of improving the fairness of the administrative process was carried out.

The Court did not deal with the fact that the Commission was required also to have substantial evidence to sustain the findings which it assumed to make (Administrative Procedure Act § 10, (e), 5 U. S. C. § 1009 (e)). The Commission in effect sought to bolster its position by referring to the fact that it did not have reparation authority. Such lack of authority cannot grant additional authority. The remedy for the lack of authority is an address by the Commission to the Congress (*Federal Power Commission* v. *Panhandle Eastern Pipe Line Co.*, 337 U. S. 498, 508, 514, 515-516 (1949)). How was it possible for a finding to be made at that stage of the case that there was "an unjust exaction was being demanded from the gas users" as the Court recites in its opinion? Petitioner respectfully states to the Court that if such a finding had been made before the evidence was presented to the Commission, there could be no substantial evidence to support the Commission's conclusion. Also such action by the Commission is analogous to the avoidance of presentment to and indictment by a grand jury before a criminal prosecution because a tribunal which is to be the ultimate trier of facts decides that the culprit is guilty.

As Judge Bratton, in his special concurrence recognized, omission is "warranted only where the Commission makes a well-founded and sustainable finding that due and timely execution of the functions of the Commission imperatively and unavoidably so requires". Judge Bratton's opinion states the problem very well and notes particularly that if a lack of reparation authority is an excuse for omitting the intermediate decision, then such decision could be omitted in every rate proceeding before the Commission, since it has no reparation authority in any instance.

The Court also seeks support in two cases for its decision here. The [illegible] *United States*, 103 F. Supp. 971 (D. C. N. J. 1952), in that case the Court noted that no objection had been made to omission of the intermediate decision and that petitioner

were error if was merely a procedural one. The Court in the *Kenny* case laid particular stress upon this fact. Of course a procedural irregularity can be waived (*United States et al. v. A. Tucker Truck Lines, Inc.*, 344 U. S. 33 (1952)).

The Court also cites *Alabama-Tennessee Natural Gas Company v. Federal Power Commission*, 203 F. 2d 491 (C. A. 3d, 1953). In that case there appeared to be reasons which were certainly more cogent than the ones in the case at bar for omitting the intermediate decision since irreparable harm could have resulted in certain of the gas company's customers being unable to meet financing commitments (see Petitioner's "Motion for Leave to File Reply to Statement of Respondent and Reply to Statement" filed with this Court, pp. 8-10). Also, in the *Alabama-Tennessee* case there was an implied consent to the omission of the intermediate decision because of the history of the case. Petitioner submits to the Court that these two cases do not support the Court's conclusion.

B. Credibility Was Involved in This Rate Proceeding

The second main ground for the Court's affirmance of the omission of the intermediate decision was its conclusion that credibility was not an issue. The Court does this on the understandable basis that all that is submitted in a case of this type is statistical data from which inferences and conclusions are to be drawn. Petitioner respectfully submits to the Court that such is not the case. One prime example was given to this Court where credibility was involved. The most important Commission Staff witness in this proceeding was determining what were normal expenditures for the Company. He as an expert was drawing the inferences and upon such determinations the Commission was asked to act. During such inquiry this witness was most hesitant and reluctant, even to the point of admonishment from the Trial Examiner (R. 1260-1262, Print 292-294). This is merely one example.

Going to the Commission's opinion and order which was brought here for review, it is evident that the Commission weighs the recommendations of witnesses. For instance, the Commission would not allow a projected 4% wage increase which Company witnesses concluded should be allowed (R. 4577, Print 86). The same is true of employee benefit proposals (R. 4578, Print 86) and other like items. The Commission allowed additional royalties to the Company as recommended by a Company witness though not on the Company's books (R. 4588-4589, Print 91-92). The Commission then went on to take the Staff recommended adjustments and noted that the Staff eliminated certain items of expense as nonrecurring. In regard to these adjustments the Commission followed the Staff. By following the Staff's recommendations it was

without saying that the Commission attached considerable importance to them (R. 4590-4591, Print 92-93).

On the all important question of the 5c wellhead value for income tax depletion the Commission followed its Staff's recommendation (R. 4593-4598, Print 94-97). In the all important question on the loss on gasoline operations the Commission did not make an independent determination but followed its Staff's recommendations (R. 4608-4619, Print 102-112). These matters occur from perusal of the Commission's opinion and order in this case. The Staff recommendations undoubtedly are of great importance to the Commission. Whether this is right or wrong Petitioner does not argue here. It is proper, however, that such recommendations be subject to the screening of the man who heard the recommendations made from the witness stand. Except in very unusual circumstances, if the recommendations of Staff are not evaluated by observance of the witness' demeanor, their weight and credibility are never thrown into the balance. This Court recognized in its opinion that the weight to be accorded to a witness' opinion is important, although it decided that credibility was not involved. Petitioner submits that the weight to be accorded a witness' opinion may well be affected by evident reluctance to testify and an evident lack of confidence in the recommendations made. As a matter of fact, credibility of a witness and the weight to be accorded to his opinion are practically inseparable labels. This certainly appeared to be recognized by the Supreme Court in the *Universal Camera* case (*supra*) where the Court held (at pp. 496-497) as follows:

> "The findings of the examiner are to be considered along with the consistency and inherent probability of testimony. The significance of his report, of course, depends largely on the importance of credibility in the particular case. To give it this significance does not seem to us materially more difficult than to heed the other factors which in sum determine whether evidence is 'substantial'".

C. This Petitioner and This Court Were Deprived of an Important Part of the Record by the Omission of the Intermediate Decision

As the Supreme Court recognized in *Universal Camera Corporation v. National Labor Relations Board* (340 U. S. 474 (1951)), the report of a trial examiner is an important part of the record from which substantiality of evidence may be gauged. Recently, this was recognized by the Eighth Circuit when it reversed a Federal Power Commission rate determination order on account of the Commission's failure to include in the record the hearing briefs filed by the parties to the rate proceeding. In determining that the Commission's findings were inadequate, the

Court matched against the Commission's determination; relevant testimony, the finding of the preceding examiner, the testimony of the Commission's expert witness, and the fact that no witness testified as to a rate of return as low as that which the Commission found (*State Corporation Commission of Kansas* v. *Federal Power Commission*, 206 F. 2d 690, 722-723 (C. A. 8th, 1953)). It is apparent that the Eighth Circuit treated the finding of the examiner as a matter of importance commensurate with the evidence of record. Here this Petitioner and this Court would never have such valuable aid in determining reviewability and thus are deprived of a very real "tool of decision".

This fact emphasizes the importance of the intermediate decision and the fact that it should not be dispensed with except for the strongest possible reasons based upon adequate evidence.

Ground Two

The Court erred in not reversing the Commission's determination on rate of return since the Commission did not make adequate factual findings but mechanically followed a mathematical formula without exercising its judgment as required by law, and also since the Commission considered undisclosed facts not in this record.

A. The Commission Must Do More Than Follow a Mathematical Formula in Determining Rate of Return

In the recent decision of the United States Court of Appeals for the Eighth Circuit which reviewed a determination of the Federal Power Commission of the rates of Northern Natural Gas Company (*infra, note, State Corporation Commission of Kansas* v. *Federal Power Commission*, 206 F. 2d 690 (1953)) it was determined that Northern Natural was entitled to a return of 5.5% by following exactly the same method used in the case at bar. The Court held that such bare findings are insufficient and remanded the case on this ground. The Eighth Circuit pointed out numerous cases which disclosed that broader considerations should be given than was the case with the Commission's treatment of Northern Natural and cited at length cases in which consideration was given to practical matters affecting the application of the practical expert judgment of the Commission.

While the Court here states that this Eighth Circuit case is distinguishable, Petitioner respectfully submits that it is not distinguishable in substance or in principle. The fundamental difficulty in the *Northern Natural* case was the fact that the Commission had followed a mathematical formula based upon historical cost of money. The same is true in the case at bar. The Commission subsequent to the holding and remand of the Eighth Circuit used

the historical cost of money but then recognized that it had a responsibility beyond this point. It cited the opinion of the Eighth Circuit and also *Bluefield Waterworks & Improvement Company* v. *Public Service Commission*, 262 U. S. 679, 695 (1923) and attended particularly to the following pronouncements of the Supreme Court:

> "What annual rate will constitute just compensation depends upon many circumstances and must be determined by the exercise of fair and enlightened judgment, having regard for all relevant facts. . . . The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties" (262 U. S. 679 at 692-693 (1923)).

The Commission, therefore, has recognized a responsibility which it did not exercise in the case at bar.

This Court has stated that the Eighth Circuit case is distinguishable from the one at bar. It is interesting to note, however, that the Commission apparently does not share this view. The Commission has filed in the Supreme Court of the United States a cross-petition for a writ of certiorari directed to the Eighth Circuit in the *Northern Natural* case on the rate of return point and in said petition states: "The decision below [Northern Natural] conflicts in principle with decisions of the United States Court of Appeals for the Tenth and District of Columbia Circuits . . ." and cites the holding of this Court in the case at bar. The Commission quotes at length from this Court's holding and states in a footnote near the end of its discussion that: "The Tenth Circuit referred to the opinion below in the instant case as 'distinguishable' but without stating in what respect." *

Petitioner submits that the findings of fact or rate of return in the instant case are not sufficient to sustain the Commission's conclusion. As the Eighth Circuit has pointed out, and as numerous other cases have pointed out, facts beyond the mere makeup of a company's capitalization and "bare bones" cost of money, must be taken into consideration and the Commission must find such additional facts as indicate an exercise of its practical judgment.

* This cross-petition of the Commission for certiorari is No. 469, October Term 1953 *sub nom. Federal Power Commission* v. *Northern Natural Gas Company, et al.* The portions referred to above occur at pp. 16-18 of said petition.

B. The Commission Considered Facts Not in This Record

There can be no doubt but that this Court is of the opinion that the Commission gave consideration only to factors of the financial history of nine unspecified natural gas companies subject to the Commission's jurisdiction and seven natural gas companies whose common stock was traded on recognized exchanges in determining the investor's appraisal of common stock requirements. Petitioner desires again to call to the Court's attention that these nine natural gas companies are unknown. These are nine out of one hundred thirty-five natural gas companies which report to the Commission (see Federal Power Commission, *Statistics of Natural Gas Companies*, 1950, p. 1). Petitioner respectfully represents that with this fact in mind the Court should not state the ready ability of Petitioner to ascertain the identity of these companies. Apparently the Court was of the impression that only these nine reported to the Commission since it stated in respect of the fact that their identity was not disclosed in the record that: "They are, however, *the* nine gas companies reporting to the Federal Power Commission . . ." (emphasis added to the definite article "the"). Petitioner submits, therefore, that reliance upon such a volume of 135 companies and extracting therefrom an unknown nine does not accord to Petitioner a fair consideration and a fair hearing.

Conclusion

The grounds put forth by this conditional cross-petition are of substantial importance. Petitioner does not request a grant of rehearing unconditionally, but Petitioner is advised and believes that the Commission is filing a petition for rehearing and upon such belief this cross-petition is filed. Petitioner does not desire that it be awarded rehearing upon the grounds set forth herein unless rehearing is granted to the Commission. Petitioner is doing this on such conditional basis because of the desirability of bringing this litigation to an early conclusion. It is requested, therefore, that this cross-petition for a rehearing be granted if the petition of the Commission is granted.

Respectfully submitted,

James Lawrence White,
William A. Dougherty,
John P. Akolt, Sr.,
John R. Turnquist,
Charles E. McGee,
Lewis M. Poe,
Counsel for Petitioner,
Colorado Interstate Gas Company

Certificate of Counsel

I hereby certify that the foregoing petition is filed in good faith and not for any purpose of delay.

James Lawrence White,
Counsel for Petitioner,
Colorado Interstate Gas Company.

Order Denying Petitioner's Petition for Rehearing

Forty-First Day, November Term, Wednesday, January 13, 1954. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard on the petition of petitioner for a rehearing herein and was submitted to the court.

On consideration whereof, it is now here ordered by the court that the said petition be and the same is hereby denied.

Opinion on Rehearing

[January 25, 1954]

William A. Dougherty (James T. White, John P. Akolt, Sr., John R. Turnquist, Charles E. McGee and Lews M. Poe with him on the brief) for Petitioner;

J. Goldberg (Willard W. Gatchell and Reuben Goldberg were with him on the brief) for Respondent.

Before Bratton, Huxman and Murrah, *United States Circuit Judges.*

Huxman, *Circuit Judge.*

We reversed the Commission's order in the above entitled cause on the ground that it erred in excluding from the cost of service base the loss resulting from the gasoline operations as set out in the opinion[1] and remanded the case for further consideration.[2] We granted the Commission's petition for rehearing because of its contention that we were without jurisdiction to consider that question sua sponte since it was not first presented to the Commission by Colorado in its petition for rehearing. In support of its position the Commission relies upon 15 U. S. C. A. § 717r (b) which in part provides as follows: "* * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing * * *."

[1] The loss as found and deducted by the Commission was fixed at $121,537.

[2] See opinion filed October 29, 1953.

It is not correct, as stated by the Commission, to say that Colorado did not object to the exclusion of this item. It did object thereto both in the original proceeding and in its petition for rehearing. It is true, however, that it did not place its objection on the legal ground upon which we predicated our conclusions.

But aside from that we think that in reviewing the Commission's order we have inherent power to consider and correct manifest and substantial error appearing in the record which leads to an unjust end result and deprives Colorado of the opportunity of earning that which the laws says is its right, namely, a fair return on its investment.

As pointed out in our original opinion, the test laid down by the Supreme Court in all its decisions in which orders of the Commission are to be gauged is the end result test. The principle laid down in those decisions is that if after a consideration by a reviewing court of the order the end result is just and gives the company a fair return on the investment the order will stand. To hold that a reviewing court is by technical rules of procedure before the Commission deprived of the opportunity to view a case in the light necessary to bring about a just end result is to destroy the rule and such a conclusion should not be reached in the absence of clear express language to that effect.

Neither do we interpret Section 717r (b) to mean that a reviewing court is deprived thereby of its right to consider all relevant matters necessary to determine a just end result. We interpret the pertinent language of the Section to mean that one complaining of the order of the Commission will not be heard and has no standing to urge an objection not first submitted to the Commission. We do not interpret *Panhandle* v. *Power Commission*, 324 U. S. 635, to hold that a reviewing court may not of its own volition consider fundamental error preventing a just end result. That was not the theory upon which the case was decided in the Circuit Court. It was decided there upon a consideration of the whole case. The Supreme Court in its opinion did say that the gas company by failing to object in its application before the Commission was precluded from raising the objection in the reviewing court, but it did not expressly hold that the Circuit Court erred in considering the case upon its merits. In fact, the Supreme Court likewise considered the case upon its merits and concluded that the end result was just. It would seem that if the court was without jurisdiction to consider the merits all that was said with respect to the merits was obiter and should have been omitted from the opinions.

United States v. *Howard Trail Lines*, 324 U. S. 774; *National Labor Relations Board* v. *Denver Coca-Cola Bottling Co.*, 317 U. S. [illegible] and *Interstate Commerce Commission* v. *Jersey City*, 322 U. S. 503 are cited by the Commission in support of its position

that we lack jurisdiction to consider the question in issue. The *Hancock Truck Line* case arose under the Interstate Commerce Act upon an application for a certificate of convenience to operate truck lines. The Commission granted a limited certificate, limiting it in operation to traffic moving on bills of lading of freight forwarders. The applicant filed an application for reconsideration in which it stated, "we do not challenge, nor do we complain against, the restriction to serve only freight forwarders." The Commission denied the other relief requested. The applicant then brought an action to enjoin only so much of the court's order as restricted its application to traffic moving on bills of lading of freight forwarders. A three-judge court issued a permanent injunction. The Supreme Court held that having expressly waived any objection to this part of the order, the carrier was estopped from urging it and it was improper for the court to reverse the Commission's order in respect to a provision therein as to which the litigant had advised that body that it no longer objected but acquiesced.

The *Cheney Lumber Company* case arose under the National Labor Relations Act. That Act contains a provision similar to Section 717r (b). Proceedings under the National Labor Relations Act involve problems materially different from those that arise under the Natural Gas Act. That Act concerns itself with facts constituting unfair labor practices. When the facts are once established, the remedy flows as a matter of law. What the court there did was to make a finding of fact with respect to an issue not submitted to the Board and that the Supreme Court said it could not do. But we are not considering for the first time an issue of fact. The loss from the gasoline operation is an established fact and we accept it. We only inquire as to the legal consequences flowing therefrom and what was the Commission's legal duty after having found the fact. So also in the *Aragon* case, supra, the reviewing court for the first time made a finding of fact with respect to a fact issue not submitted to the Employment Compensation Commission.

Furthermore we are of the view that our conclusion that we have inherent power to sua sponte note basic erroneous legal conclusions adduced from established facts is strengthened by Section 10 of the Administrative Procedure Act, 5 U. S. C. A. § 1009, which in part provides that "So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions * * * It shall * * * hold unlawful and set aside agency action findings and conclusions found to be * * * not in accordance with law; (2) contrary to constitutional right, power, privilege or immunity * * *
To begin with we are at a loss to consider the legality or appropriateness of the action of an administrative agency based upon

facts found by it and unchallenged in the reversing court, would seem to make nugatory and meaningless those clear and positive mandates of the Section.

It is also of some significance that of the cases relied upon by the Commission, *Cheney Lumber Company*, and *Hancock Truck Lines, Inc.*, were decided prior to the passage of the Act and, while the *Aragon* case was decided approximately three months after the effective date of the statute, it did not revolve around a provision such as we had under consideration. For these reasons, we adhere to the views expressed in our original opinion.

On the argument on the petition for rehearing it was stressed that prior to the merger order Colorado received all the net revenue from the gasoline operations but that under the merger order it relinquished fifty per cent of such revenues and still bears all the cost thereof and that this is unjust to Colorado's consumers. Our opinion to remand did not indicate the treatment to be accorded to this item of cost of service. All we required was that it be considered as an element of cost of service in light of all the facts of the case.

The order of the Commission is, therefore, REVERSED and the cause is REMANDED for further proceedings in accordance with the views expressed herein.

JUDGMENT

Forty-Ninth Day, November Term, Monday, January 25, 1954. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard on rehearing and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the order of the Federal Power Commission in this cause be and the same is hereby reversed, and that this cause be and the same is hereby remanded to the said Federal Power Commission for further proceedings in accordance with the views expressed in the opinion of the court.

On February 3, 1954, an order of the United States Court of Appeals was entered staying the mandate of the said court to April 1, 1954, under provision of paragraph 3 of rule 28 of said court.

ORDER RE DEPOSIT IN ESCROW ACCOUNT

SIXTY-SEVENTH DAY, NOVEMBER TERM, FRIDAY, FEBRUARY 26, 1954. Before Honorable Sam G. Bratton, Circuit Judge.

This matter coming on for consideration upon the motion of Colorado Interstate Gas Company, Petitioner herein, for a temporary deferment of the payment due to be made by it into the Escrow

Account in the First National Bank of Denver on February 25, 1954, under previous orders entered in this proceeding on September 8, 1952, and October 7, 1952.

It appearing to the Court that the Federal Power Commission, acting through its attorneys, has consented to the allowance of said Motion, and it further appearing that no prejudice will result from the granting thereof, and that there is good cause therefor,

It Is Ordered, Ordered that pending the further order of this Court, Petitioner be and it hereby is granted a determent from the 25th day of February, 1954, to the 15th day of March, 1954, in which to deposit in the Escrow Account in the First National Bank of Denver the sum of money which otherwise would have been deposited in such Account on said February 25, 1954, under the provisions of the prior Orders of this Court entered herein on September 8, 1952, and October 7, 1952.

Except to the extent herein modified said Orders of September 8, 1952, and October 7, 1952 shall remain in full force and effect until the further order of this Court.

Entered this 25th day of February, 1954.

STAY ORDER

Seventy-Seventh Day, November Term, Monday, March 15, 1954. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause this day coming on for consideration by the Court upon the petition of Colorado Interstate Gas Company for modification of orders of this Court issued September 8, 1952 and October 7, 1952, staying a rate order of the Federal Power Commission issued August 8, 1952, in said Commission's Docket No. G-4115 pending judicial review; and it appearing to the Court that said Petitioner has filed on September 2, 1953 new rates with the Federal Power Commission which were suspended to the extent permitted by the Natural Gas Act, and the suspended rates have been permitted to become effective on January 1, 1954 subject to refund; and it further appearing to the Court that said rates filed on September 2, 1953 are the presently effective rates of Petitioner, subject only to final determination and order of the said Commission; and it further appearing to the Court that Petitioner and the Commission have stipulated and agreed that an undertaking may be filed by Colorado with the said Commission which will obligate Colorado to refund from and after January 1, 1954, any difference between the rates finally effective in Commission Docket No. G-4115 and the rates made effective on January 1, 1954, in Docket No. G-2208, and the Court having otherwise considered the petition and other documents filed herein does find that it is desirable that said Petitioner be relieved from and after January 1, 1954, as

the condition of the stay orders above recited which provided for deposit in escrow of the difference between the refund rates prescribed by said Commission in its said Docket No. G-2115 and those previously in effect; and it further appearing to the Court that no prejudice will result from such relief pertained for;

It Is Now, Therefore, Hereby Ordered that the paragraphs of said stay orders which recite the conditions of the stay be amended, and the same hereby are amended by removing therefrom those portions of said paragraphs imposing conditions which are designated in each thereof as (1c, 2c, 4c and 5c, it being understood, however, that such amendment and deletion shall be deemed to be effective only from and after January 1, 1954, and that the provisions of said orders are otherwise to remain in full force and effect.

On March 23, 1954 an order of the United States Court of Appeals was entered staying the mandate of the said court to May 1, 1954, under provisions of paragraph 3 of rule 28 of said court.

Clerk's Certificate

United States Court of Appeals, Tenth Circuit

I, Robert B. Carwright, Clerk of the United States Court of Appeals for the Tenth Circuit, do hereby certify the foregoing to be a full, true, and complete copy of the designated transcript of the record from the Federal Power Commission, and full, true, and complete copies of certain pleadings, record entries and proceedings, including the opinions (except full captions, titles and endorsements omitted in pursuance of the rules of the Supreme Court of the United States) had and filed in the United States Court of Appeals for the Tenth Circuit in a certain cause in said United States Court of Appeals, No. 15 [illegible], wherein Colorado Interstate Gas Company was petitioner, and the Federal Power Commission was respondent, as full, true, and complete as the originals of the same remain on file and of record in my office.

In Testimony Whereof, I hereunto subscribe my name and affix the seal of the United States Court of Appeals for the Tenth Circuit, at my office in Denver, Colorado, this 31st day of March, A. D. 1954.

Robert B. Carwright
Clerk of the United States Court
of Appeals, Tenth Circuit

By /s/ George A. Pfaff
Chief Deputy Clerk

[Seal]

ADDITION TO RECORD

Filed, United States Court of Appeals Tenth Circuit, January 4, 1954. Robert B. Cartwright, Clerk.

United States Court of Appeals Tenth Circuit

No. 4541

COLORADO INTERSTATE GAS COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT, CITY AND COUNTY OF DENVER, AND PUBLIC UTILITIES COMMISSION OF COLORADO, INTERVENORS

BRIEF OF PETITIONER IN RESPONSE TO RESPONDENT'S PETITION FOR REHEARING

Pursuant to the order of the Court entered on rehearing, Petitioner responds to the arguments and grounds set forth by the Federal Power Commission ("Commission") in its petition for rehearing.

Inasmuch as the matter being considered by the Court arises from the Court's action, no statement or counterstatement of the case as such should be necessary.

INTRODUCTION

The perspective of this case is that Petitioner brought here for review the Commission's rate determination. The Commission in its petition for rehearing states that there was "No objection to the exclusion of the loss on gasoline operations from cost of service was raised by Petitioner at any time before the Commission during the administrative rate proceedings or before the court" (p. 3). This is erroneous. This Court, of course, recognizes and dealt with the fact that Petitioner

claimed that there should be no exclusion from the cost of service of any loss on gasoline operations. While Petitioner did not argue the very ground pointed out by the Court for reversal, nevertheless, there was before the Court a record for review of the rate proceeding, and in it was the issue of deducting the Commission found loss on gasoline operations. It can be well understood why Petitioner did not urge as a ground of reversal the ground adopted by the Court. Petitioner having acquiesced in the condition which the Court has struck down could hardly immediately turn its back upon such acquiescence. The Court struck at the heart of the matter and declared the merger condition invalid. Respondent can now act on the basis of that clear and correct legal pronouncement and in so doing can justify the Court's action.

1. This Court had the power on its own motion to consider the propriety of the condition involved and to reach the result of its judgment

The Commission asserts from the beginning a limitation upon the Court's power arising by virtue of Section 19 (b) of the Natural Gas Act (52 Stat. 831, 15 U. S. C. § 717r (b)). The Commission cites several cases which it must contend support its view that this Court was limited in its powers of review to the point where it could not strike down the illegal condition. These cases will be dealt with below. It is odd, but understandable, that the Commission has approached this fundamental problem backwards. Petitioner submits that the proper approach is first to determine what a reviewing court's powers really are. This is not difficult since there are many authoritative pronouncements, and in the light of judicial authority it will be seen that even the cases cited by the Commission support this Court rather than negate the power which the Court has exercised.

It is recognized that ordinarily an appellate court does not give consideration to issues which were not raised below, but as the Supreme Court has stated this is subject to exceptions of materiality in the instant case:

> There may always be exceptional cases or particular circumstances which will prompt a reviewing or appel-

> late court, where injustice might otherwise result, to consider questions of law which were neither pressed nor passed upon by the court or administrative agency below.

and further:

> Decisions not in accordance with law should be modified, reversed or reversed and remanded "as justice may require" (*Hormel* v. *Helvering*, 312 U. S. 552 at 557 and 559 (1941)).

This rule has been recognized by this very circuit when in *Smith* v. *Welch*, 189 F. 2d 832 at 836 (1951) the Court stated:

> While we recognize the power of an appellate court in a proper case to consider on its own motion errors to which no objections were made, it should be exercised sparingly and only in exceptional cases and in the interest of justice.

Indeed, the very Judges of this Court who made the determination in the instant case that the condition was invalid have recognized this authority in *E. I. Du Pont De Nemours & Co.* v. *Cudd*, 176 F. 2d 855 (1949) and stated (per Judge Huxman) at 857 that:

> Appellate courts have inherent power to correct substantial error occurring during a trial even though not directly raised. In referring to the general rule that one who has not appealed may not as a matter of right, question the correctness of the court's judgment, the Supreme Court in Langnes *v.* Green, 282 U. S. 531, 538, 51 S. Ct. 243, 246, 75 L. ed. 520, states "these decisions simply announce a rule of practice which generally has been followed; but none of them deny the power of the court to review objections urged by respondent, although he has not applied for certiorari, if the court deems there is good reason to do so." [1]

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[1] To the same effect also are: *Public Service Commission* v. *Havemeyer*, 296 U. S. 506 (1936); *Shaw* v. *Addison*, 236 Iowa 729, 18 N. W. 2d 796, 803; *Clark* v. *Wells E. Coal Co.*, 215 Ky. 128, 284 S. W. 91, 93; *Curry* v. *Dahlberg*, 341 Mo. 897, 110 S. W. 2d 742.

Illegality of a contract—certainly analogous to the situation here—seems to be a particularly appropriate place for a court to refuse to occupy the anomalous position of giving judicial support to illegality (see note, Raising New Issues on Appeal, 64 *Harv. Law Review*, 652, 661).

Obviously, the Commission has confused (1) what a party on review can insist that the appellate court consider and (2) *what the appellate court itself can consider* and still act within proper bounds of judicial responsibility. This distinction was pointed out in *Calhoun County, Fla.* v. *Roberts*, 137 F. 2d 130 (5th Cir., 1943). In that case the Court stated:

> We acknowledge the general rule that a cross appeal or cross certiorari is necessary to enable an appellee or respondent in certiorari to ask the appellate court to reverse the part of a decree which is unfavorable to him. Morley Construction Co. *v.* Maryland Casualty Co., 300 U. S. 185, 57 S. Ct. 325, 81 L. ed. 593. The rule was applied even to an admiralty decree, the appeal from which is a *de novo* trial, in the Maria Martin (Martin *v.* Northern Transportation Co.) 12 Wall. 31, 20 L. ed. 251. But in another case in admiralty, Langnes *v.* Green, 282 U. S. 531, 51 S. Ct. 243, 75 L. ed. 520 by way of considered dictum, it was declared that the rule is one of the practice generally followed, limiting the rights of litigants, *but not a restriction on the power of the appellate court to see that justice is done*. We are reversing the conclusion of law of the district Judge that the recourse is against the County and we esteem it necessary to justice to reopen his conclusion of law that there was no recourse against any hand proceeds in the balance of the Construction Fund. *We act on our own motion, and not at the instance of appellee.* We have disturbed no fact finding of the district court (as was done in the Morley Construction Company case) but differing only on the law, we propose to apply in all its consequences the law as we see it. We hold we have the power, without cross appeal, to do this (*id.* 132). [Italics added].

The argument of the Commission also overlooks the important remedial legislation of the Administrative Procedure Act. Section 10 (e) of that Act (5 U. S. C. § 1009 (e)) imposes upon the reviewing court a duty to review the whole record. As the Senate Committee in considering that legislation stated:

> The requirement of review upon "the whole record" means that courts may not look only to the case presented by one party, since other evidence may weaken or even indisputably destroy that case (Senate Committee Report, 1945, p. 28; Senate Document No. 248, 79th Cong., p. 214).

The Sixth Circuit had occasion to deal with this requirement and to study the legislative history above quoted in *Pittsburgh Steamship Co.* v. *National Labor Relations Board*, 180 F. 2d 731 (1950) and upon a remand undertook to consider a complete Labor Board record. That Court stated:

> The reviewing court is requred to hold unlawful and set aside agency action, findings, and conclusions not in accordance with law and unsupported by substantial evidence, and in making its determination it is also required to review the whole record. These mandatory provisions define and make specific the requirements of judicial review and extend them beyond the requirements of the Wagner Act (*id.* 736).

and further held:

> We therefore proceed to inquire, upon a consideration of the whole record, whether the order sought to be enforced is supported by the reliable, probative, and substantial evidence and *is in accordance with law* (*id.* 737). [Italics supplied.]

As the Court recognized in the instant case, its concern is with the "end result" of the Commission's rate determination. This end result theory certainly reached its strongest position in *Federal Power Commission, et al.* v. *Hope Natural Gas Company*, 320 U. S. 581 (1944). In announcing the doctrine that it is the impact rather than the theory of the rate determination which counts, the Supreme Court stated:

> And when the Commission's order is challenged in the courts, the question is whether that order "viewed in its entirety" meets the requirements of the Act (*Id.* 602). (See also *Federal Power Commission* v. *Natural Gas Pipeline Company*, 315 U. S. 575, 586 (1942).)

The question of whether or not the Commission under the merger condition was making a deduction from Petitioner's rate of return was fundamental and without possibility of refutation affected the fairness of the end result of the Commission's order. To allow a regulated business less than a fair return has been recognized as confiscation prohibited by the Constitution for so long a time that authority to such effect need not be cited. The Commission under the Natural Gas Act certainly had no greater latitude. The Supreme Court in the *Hope* case (*supra*) at page 607 stated:

> Since there are no Constitutional requirements more exacting than the standards of the Act, a rate order which conforms to the latter does not run afoul of the former.

With the fundamental nature of the question thus noticed by the Court, the Court quite properly in furtherance of its judicial duty recognized its obligation and acted accordingly. It does no good at this posture of the case to attempt to upset the Court's conclusions on the basis of the fact that the issue was not presented to the Court by any party. If the Court had power to do what it did without argument on the specific point, the matter is at an end.

Petitioner recognizes that in the ordinary review one is limited to those errors which have been presented below. The Supreme Court in dealing with a review provision of the National Labor Relations Act similar to those involved under the Natural Gas Act has stated that this limitation "gives emphasis to the salutary policy adopted by Section 10 (e) [of the National Labor Relations Act] of affording the Board opportunity to consider on the merits questions to be urged upon review of its order" (*National Labor Relations Board* v. *Cheney California Lumber Company*, 327 U. S. 385 (1946) at 389; *Marshall Field & Company* v. *National Labor Relations Board*, 318 U. S.

253, 256 (1943)). To like effect is *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143 (1946).

Both the *Aragon* case and the *Chenery* case are cited by the Commission in support of its contentions. The short answer is that the merger condition had already been considered by the Commission in the merger proceedings. The condition was a subject of the Commission's opinion in such case (R. 2740, p. 561) and was a specific part of the Commission's order (R. 2776, p. 566). Furthermore, a dissenting Commissioner in that case seriously questioned the validity of the condition which the Court has struck down.[2] The merger condition, and the consideration of its validity is part of *this* record.

In addition, the Commission's counsel in the merger case in oral argument before the full Commission stated unequivocally that such condition would not be enforceable.[3]

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[2] Commissioner Buchanan in his dissent stated the following:

"These conditions, while devised to afford some protection to consumers against the natural consequences of the majority's action in approving the merger actually, in my opinion, have no such effect under the law. Should Colorado fail to earn a fair return in the future, the natural gasoline revenues given up to Southwestern cannot be treated as revenues of Colorado. They are gone forever. I question seriously whether the stockholders of Colorado can be compelled to accept a confiscatory rate of return simply because of a condition inserted in a certificate by the Federal Power Commission and accepted by their present Board of Directors. The present stockholders of Colorado, with the exception of Public Service, expect to distribute all of their holdings of Colorado's stock to the public as soon as the merger is consummated. The new stockholders will expect to be adequately compensated for their investment" (R. 2771).

[3] Lambert McAllister, Esq., for the Staff of the Commission had the following to say:

"As a matter of corporate law, neither Mr. Daugherty [*sic*] or the Board of Directors can bind the stockholders down through the future so that they would be cut by that agreement to a return of 4 per cent."

Immediately following this statement, there was the following exchange between Commissioner Smith and Mr. McAllister:

"Commissioner SMITH. Mr. McAllister, a moment ago you mentioned Mr. Daugherty's [*sic*] offer of a stipulation or something of the sort and you said it would not be worth anything if the Commission tried to fix a rate as low as 4 per cent and of course that is obviously true. It would be a rate at the point of confiscation.

"You do not contend, do you, that the Company could not be bound by the acceptance of a condition which would prevent it from making a claim in a rate proceeding for a given amount of revenue, do you?

Mr. MCALLISTER. Yes, I do, Mr. Chairman. I just don't think that a board of directors, particularly in this case when both Union Security is

The condition, therefore, was considered by the Commission and even if the Court be deemed to lack the fundamental power to review on its own motion the validity of the condition not assigned as error below, the reason for denying this power would be gone since the "salutary" purpose of Section 19 (b) of the Natural Gas Act would be satisfied. The Commission was not denied opportunity to consider validity. Validity was put to it as squarely as possible in the merger case.

The Commission in support of its contentions cites the *Aragon*, *Cheney* and *American Power & Light* cases. If these cases are appropriate at all, they cannot under the facts support the Commission since the Commission had the opportunity to, did consider, and did act upon the merger condition. Its invalidity was asserted and must per force be considered as having been before the Commission for determination. The Commission also cites on its behalf *Panhandle Eastern Pipe Line Company* v. *Federal Power Commission*, 324 U. S. 635 (1945). That case preceded the Administrative Procedure Act. That case also did not involve the fundamental problem of reducing the Company's return by the simple device of not allowing to it all incurred costs. The Commission also cited *United States* v. *Hancock Truck Lines, Inc.*, 324 U. S. 774 (1945) for the proposition that Petitioner's acquiescence in the condition bound it. The acquiescence in the *Hancock* case was to a restriction of routes of a truck line in a certificate order of the Interstate Commerce Commission. This again was not so fundamental as a reduction of what the Commission otherwise determines is a

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owning 42.5 per cent and South Western has 42.5 per cent. This is 85 per cent of the common stock. The two companies agree there at the stockholder level and then they move up to Colorado Interstate, at the board level, and all the way they agree on an arrangement which might result in 4 per cent in the future to them. Then when that has been done, they scatter the stock to the four winds—85 per cent of Colorado Interstate. I am certain there is no court in the land that would hold those future stockholders or their representatives to a 4 per cent return because of some arrangement that someone speaking on behalf of the company, even with the approval of the board of directors, might undertake to bind that company. It could not be done. Nor could this Commission bind a future Commission to do that thing." (Transcript of Record, FPC Docket No. G-1326, In the Matter of Colorado Interstate Gas Company and Canadian River Gas Company, pp. 1783-1785.)

fair rate of return. Acquiescence in the denial of a fundamental or Constitutional right is without effect (*Southern Pacific Company* v. *Denton*, 146 U. S. 202 (1892)). In the *Denton* case the State of Texas attempted to take away a foreign corporation's right to resort to a Federal court in diversity cases as a condition to doing business in Texas. The Supreme Court would not allow this statutory restriction to deny the foreign corporation its fundamental right.

There is another important factor involved in this regard, *i. e.*, that this previous consideration by the Commission gives reasonable excuse for failure to urge the invalidity of the merger condition before the Commission in the rate proceeding itself (*Cf. American Power & Light Company* v. *Securities & Exchange Commission*, 141 F. 2d 607 (1st Cir. 1947)).

The plain conclusion, therefore, is that the Court had the power and authority and, perhaps, even the positive duty to make its inquiry in the instant case. The Court acquired the jurisdiction judicially to review this rate proceeding. A portion of the Commission's complaint is that it had no opportunity to present its side of the case on this question. The Court by granting rehearing has afforded this opportunity; therefore, no objection in that direction now lies. The contentions in respect of the invalidity of the condition were, as a matter of fact, actually in the record of the case since the opinions in the merger proceeding were made a part of this record (Item A. R. 2722 *et seq.*, p. 549 *et seq.*).

Petitioner assigned as error in its application for rehearing that the end result as proposed by the Staff and as adopted by the Commission was unfair, unjust and amounted to confiscation (R. 4660, pp. 154-155). Petitioner in great detail challenged the Commission's deduction of an alleged loss on natural gasoline operations and, in fact, averred that the Commission's treatment amounted to a reduction in the rate of return (R. 4680-4681, pp. 176-177).

To sustain the Commission would mean that this Court lacks the power which the numerous cases cited above indicate that it has. To sustain the Commission would mean that this very panel of the Court was in error in the *Du Pont* case, *supra*. Petitioner submits that the Court has the power to do what it

did. It has this power as an inherent adjunct of the power to review under existing law. The contentions advanced by the Commission on not raising the problem below are met, even if it be assumed, arguendo, that the Court did not have the power on its own motion since the validity of the merger condition had been previously considered by the Commission and the condition was imposed.

2. There was no collateral attack

The Commission contends that this Court acted in error because on the basis of an unjust end result the Commission's order was reversed. Petitioner has pointed out above that under the "end result" doctrine, in a court of general review (as contrasted with the Supreme Court on limited certiorari) there is a judicial obligation to view the order in its entirety. The Commission does not meet this Court's rationale which clearly announces and follows its important judicial obligation.

As a matter of well recognized legal principles a previous administrative determination is not always embalmed and put beyond judicial scrutiny. As one court has recently held:

> "* * * we do not think the Commission can preserve from judicial examination a possibly erroneous legal ruling by embalming it *in res judicata*. This court, speaking through Chief Justice Groner in Churchill Tabernacle *v.* Federal Communications Commission, 1947, 81 U. S. App. D. C. 411, 160 F. 2d 244, 246, described as well settled the doctrine that 'res *judicata* and equitable estoppel do not ordinarily apply to decisions of administrative tribunals.'" *Niagara Mohawk Power Corp.* v. *F. P. C.*, 202 F. 2d 190 (D. C. Cir., 1952).*

In addition, it is indeed questionable whether the offending merger condition could have been the subject of previous review or judicial scrutiny. That condition, without possible doubt is one relating only to rates under Sections 4 and 5 of the National Gas Act (15 U. S. C. §§ 717c, 717d). The merger pro-

*The *Niagara Mohawk* case is awaiting determination by the Supreme Court. The above principle, however, or its application, are not before that Court.

ceeding was for a certificate of public convenience and necessity under Section 7 of that Act (15 U. S. C. § 717f). As the Supreme Court has held where "the order sought to be reviewed does not of itself adversely affect complainant but only affects his rights adversely on the contingency of future administrative action" it is not reviewable. The Court held that review in such case is premature (*Rochester Telephone Corp* v. *U. S.*, 307 U. S. 125, 130 (1939)). *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 581 (1944) could almost have been dealing with the instant case when it quoted the above doctrine of the *Rochester Telephone* case and stated "these findings may never result in the respondent feeling the pinch of administrative action" (*id.* at 619).

Certainly here, Petitioner may not have felt the pinch until the pinch was applied through the Commission's use of the relative market value method of allocation. Had the Commission used Petitioner's method there would have been no pinch—no aggrievement. Certainly at the time of the merger order, the pinch was only a possibility depending first upon a rate proceeding and, second, upon an allocation resulting in a showing of loss.

The Commission cites many cases in its petition (p. 8) which evidently are supposed to stand for the proposition that this Court is guilty of collateral attack. None of these cases are in point here. The appellate cases cited stand only for the proposition either that where a final order having immediate effect of aggrievement is entered the right to review ripens;[3] or a narrow statutory review under emergency legislation accords with due process or is exclusive and determinations previously made are not reviewable on enforcement;[4] or that a

[3] *Federal Power Commission* v. *Pacific P. & L. Company*, 307 U. S. 156 (1939), where it was determined that denial of a certificate of public convenience and necessity is reviewable. *Louisville G. & E. Company* v. *Federal Power Commission*, 129 F. 2d 126 (6th Cir., 1942), where orders requiring immediate action were held then reviewable. The Court recognized that preliminary orders are not.

[4] *Woods* v. *Kaye*, 175 F. 2d 886 (9th Cir., 1949); *Yakus* v. *United States*, 321 U. S. 414 (1944); *United States* v. *Ruzicka*, 329 U. S. 287 (1946); *La Verne Coop* v. *United States*, 143 F. 2d 415 (9th Cir., 1944); *Lichter* v. *United States*, 334 U. S. 742 (1948).

declaratory judgment cannot be used to review a Federal Trade Commission order;[1] or the appeal was frivolous.[2]

If the Court were to follow the Commission's prayer it could only mean that *for all time* the condition would be effective no matter how vicious its consequences to investors or how prejudicial to the public's interest in having a healthy, well regulated company attend the public convenience and necessity. Conceivably, the continued insulation of the condition from review under a doctrine of not allowing collateral attack could mean no return at all or even the possibility of not recovering otherwise reimbursable operating expenses. For all time, argues the Commission, an improvident, illegal, confiscatory condition shall exist. The Commission's prayer on this point can have no other meaning.

The Commission attempts to bolster its argument by urging that this Court's action is to grant approval of the merger without the condition (p. 9). Of course, that just is not so. The Court has done nothing but strike down the condition as an instrument for reducing the proper cost of service in a rate case. The Court in no wise has attempted to use that discretion of the Commission disclosed in *Federal Power Commission* v. *Idaho Power Company*, 344 U. S. 17 (1952) cited by the Commission.

3. The end result test does support the Court's reversal

The Commission attacks this Court's fundamental approach in reversing by citing (at p. 11) the *Hope* case and by asserting that there are two important qualifications to the proposition that from the "investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business." In the first place, Petitioner fails to discern from the *Hope* case that the qualifications asserted by the Commission were stated as qualifications by the Supreme Court. The qualifications asserted by the Commission are (a) a balancing of investor and consumer interests and (b) that there may be conditions under which more or less might be allowed to an investor without producing an unjust and unreasonable end result. The Supreme Court stated

[1] *Miles Laboratories* v. *Federal Trade Commission*, 140 F. 2d 683 (6th Cir., 1944).

[2] *Pruma* v. *United States*, 125 F. 2d 601 (9th Cir., 1942).

unequivocably: "From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock" (*Federal Power Commission* v. *Hope Natural Gas Company*, *supra* at p. 603). The Supreme Court obviously was dealing with two portions of the cost of service. The first are the operating expenses and the second is the return or a part of the return. The Court then immediately goes on to discuss what the return must be. The Court nowhere indicates that the cost of service is to be reduced because of the disallowance of legitimate operating expenses. Also, however, because of the effect of merger condition and because of the disallowance of actual legitimate expenses, the investor does not get what he is entitled to. So, therefore, when expenses are not allowed the return is affected. It is inconceivable that the Supreme Court was stating that the rate of return is such a flexible thing that operating expenses may be disallowed and yet the rate be valid because the investor has to absorb the loss. The *Hope* case can stand for nothing if it does not stand for the proposition that proper operating expenses must be allowed.

When the Supreme Court in the *Hope* case spoke of balancing the interests, it was talking about the end results of the rate making process. After stating this proposition the Court went on to state:

> But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated. From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business.

The Court was not qualifying the general proposition when it made this pronouncement; in fact, it expressly stated "But such considerations aside * * *". Secondly, the Commission asserts that the Court recognized in the *Hope* case that more or less than reasonable rates might be allowed without producing an unjust end result. The Court does not state such a qualification but merely states: "The conditions under which more or less might be allowed are not important here."

Since it is the impact of a rate determination which is important, the end result of an order which has the impact of allowing less than the actual cost of service—less than all expenses involved—is unreasonable and invalid. As the District of Columbia Circuit has stated:

> Expenses (using that term in its broad sense to include not only operating expenses but depreciation and taxes) are facts. They are to be ascertained, not created by the regulatory authorities. If properly incurred, they must be allowed as part of the composition of the rates. Otherwise, the so-called allowance of a return upon the investment, being an amount over and above expenses would be a farce (*Mississippi River Fuel Corporation v. Federal Power Commission*, 116 F. 2d 433 at 437 (1947)).

If such lesser allowance results from an invalid condition then the evil can be corrected by striking down the condition. The Court took this direct route.

The Commission argues that the exclusion of gasoline losses was a proper balancing of investor and consumer interests. The Commission's argument would indicate to the Court that what was flowing from the merger was solely or at least largely for the benefit of Petitioner's investors. This is just not the case. The record clearly shows the salutary features of the merger on benefits which would accrue to the consumers as well as to Petitioner's investors. The majority of the Commission in approving the merger stated as follows:

> A summary of the salient conclusions justified by the facts appearing on this record will demonstrate succinctly the desirability of the project laid before us for judgment:
>
> (1) The merger can be reasonably expected to cost Colorado no more than $3,062,713 spread over a 25-year period and may result in a cash benefit to it over the same period of $1,376,435.
>
> (2) Colorado will acquire legal title to physical assets, the original cost of which, after depreciation, is $10,979,522. These include natural gas reserves containing some 3 trillion cubic feet of gas which is expected to be adequate to supply the needs of the gas consumers

in the Rocky Mountain area for at least 20 years at a low cost.

(3) Colorado will gain valuable reversionary rights in the physical assets mentioned above which, but for the merger, would have matured to the benefit of Southwestern rather than Colorado probably by 1972.

(4) The corporate structure of the Texas-to-Denver pipeline will be greatly simplified with resulting savings.

(5) There will be created through the merger a financially sound natural gas company able to finance present and future expansions to meet the needs of the gas consumers dependent upon its system.

(6) The imperative need for large additional deliveries of natural gas to meet the requirements of the Rocky Mountain area, primarily those of domestic customers, will be satisfied without further unnecessary delay without any increase in present rates to the consumer.

These, then, are the principal reasons which led us to issue our certificate order of March 1, 1951. Viewing dispassionately all of the evidence in this case, we think that denial of the application would have been a distinct disservice to the public (R. 2744-2745).

It must be pointed out that the reason for proposing the merger was that Petitioner stood in need of financing in order to construct facilities required to render service to the public in the then immediate amount of $13,500,000 and the Company could not finance such project except by the merger (R. 2729-2730; p. 554-555). The Commission previously had authorized the needed construction but had withheld final approval upon the merger. The merger case was in progress for almost a year and the Petitioner was met with all sorts of obstacles. Such objection to the merger was so intense that the members of the Commission noted it (R. 2723, p. 570). [illegible] interests involved in the case and the source of the objections there should be a stipulation by the Company [illegible] from a representative of the City of Denver and [illegible] tioner's counsel as the Commission indicates. The [illegible] of testimony from the merger case on this point is [illegible] Appendix A hereto. It will be seen that the merger condition

finally sought to be imposed was different from what was originally proposed by the Company. This point is neither here nor there, however, because as this Court has recognized, this business is affected with a public interest and Petitioner was not free to contract in the unfettered fashion of a private party. The point is enlightening, however, since it shows the genesis of the condition.

The Commission seeks to bolster its position by stating that Petitioner could contract or acquiesce in fixing less than a reasonable rate and cites *Interstate Railway Company* v. *Massachusetts*, 207 U. S. 79 (1907). The Commission asserts that this case stands for the proposition that the acceptance of a charter subject to a statutory condition to transport school children at half fare prevented a utility from complaining that this was less than fair compensation. Examination of the opinion by Justice Holmes will disclose that he hesitatingly agreed with the state court's conclusion to such effect and did so only on the ground that the state was exercising its police power. As Mr. Justice Holmes put it, the question is narrowed to the magnitude of the burden and he concluded that he could not assume that the total effect of the condition would be more serious than a change in the law of nuisance might be. As the Court recognizes, the matter in the case at bar is clearly distinguishable. As this Court has stated:

> A rate based upon the exclusion from the cost of service, no matter for what reason, of a substantial amount of admitted operative cost does not and cannot reach a just end result and may, therefore, not stand.

Petitioner submits that the real applicable doctrine is that pronounced in *Augusta-Aiken Railway & Electric Corp.* v. *Railroad Commission*, 281 Fed. 977 (4th Cir., 1922), wherein it was stated:

> The Commission is without power to make rates by contract; its only power, delegated to it by the legislature, is to fix reasonable rates. * * *

Finally, the Commission gives as evidence that no unjust end result comes about the fact that an offering of stock of the Company had been oversubscribed. Suffice it to say that this oversubscription of the Petitioner's stock took place even

before these rate proceedings were concluded before the Commission and before the Commission issued its confiscatory order. Even if this were not so, the fact that the Company's stock has been oversubscribed is not conclusive one way or the other as to whether the Commission has set a just and reasonable rate.

CONCLUSION

Petitioner submits that this Court had the power and properly exercised the power in reversing the Commission, that its action in such regard is in no way a collateral attack, and the obvious unjust end result discerned by the Court justified the reversal.

Respectfully submitted.

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APPENDIX A

(Excerpt, Transcript of Testimony F. P. C. Docket G–1326, pp. 1008–1013)

By Mr. SMITH:

Q. Mr. Dougherty, is it a fact that following some discussions we had in Denver that I sent you a letter dated November 3, 1950 in which I suggested that Colorado Interstate and Canadian River might be able to satisfy the Commission concerning the proposed so-called payments to Southwestern if they would recommend treating these payments as a nonutility expense for rate-making purposes?—A. Yes, you did.

Q. And my suggestion was in effect this: That the Commission might possibly be satisfied if the companies would offer to accept a condition that these so-called payments to Southwestern be classified by the merged company in Account 538, Miscellaneous Income Deductions, for accounting and rate-making purposes, and that the concurrent credit apparently would be to Account 730.1, Residuals Produced—Credit. Was that my suggestion?—A. Yes.

Q. Then I went a head to state in support of that suggestion that it would give the Commission control over the matter for accounting and rate-making purposes and would enable it to determine reasonableness in any future proceeding in the light of known facts at the time, and that thus the balancing of investor and consumer interests could be done as frequently as necessary, perhaps with greater precision, on the basis of known facts, rather than long-range estimates.

I also suggested, I believe, that if it were found in a rate case that Colorado Interstate was actually deriving tax benefits as a result of the merger that in my opinion the Commission could properly associate those benefits with the proposed charges to Account 538.—A. Yes, you did.

Q. Do you have anything to say with respect to that suggestion at this time?—A. Well, you will recall, Mr. Smith, I

replied to your suggestion saying that in the exact manner in which you made it it did not appeal to me as something that I could recommend to Colorado Interstate Gas Company. That is, as I understood your suggestion, the accounts above the line, the operating revenues and expense accounts, would in effect be the same as if this gasoline transaction by which Southwestern would have half of the gross revenues from the gasoline had never taken place, and yet, at the same time, any reduction in income taxes that would accrue to Colorado Interstate as a result of the tax benefits that are anticipated in the event the merger takes place would be reflected in the expense accounts.

I also said, and it is my judgment, that accounting for this 50 per cent of the gross as though it were a deduction below the line—that is, other income deduction—would in the future pretty well bind the company with respect to the results of that accounting procedure.

In other words, that the Commission in the future would say that, having accounted for this gasoline transaction in the way you have suggested, whereby the full credit of the full gasoline revenues are reflected against the operating expenses of Colorado and also the full benefits of these tax reductions are reflected, it would bind Colorado as considering that this was to be treated in that manner, and that the 50 per cent of gross which would be charged to Account 538 would be treated as a non-income item without there being taken into consideration any credit for these tax benefits.

That was my answer to you. I think I either in the letter or orally stated to you that so far as I was concerned as a director of Colorado Interstate and as its counsel that I would be perfectly willing to vote for as a director and to recommend to the board as its counsel that some sort of a stipulation or condition to the certificate be accepted by the company which in effect would provide this:

Referring now to the amounts that are considered as being the gasoline revenues which are taken from the operations and which are reflected in Exhibit 38 as Sub-Exhibit B, and with respect to the tax benefits that are reflected in that same Sub-Exhibit B of Exhibit 38, that whenever those tax benefits would be less than the amount that the merged company had given

up in the way of gasoline receipts after taxes, that such difference would not be treated and should not be treated in any rate proceeding as a cost of operations or, in other words, that that difference would be borne by the stockholders, or you might say that the risk of any deficiency in those tax benefits as estimated would be assumed by the stockholders, so that the ratepayers would in no way be taking any risk, providing, of course, that wherever these tax benefits would exceed whatever had been given up in the way of gasoline revenues it would be kept for the benefit of the stockholders.

My concept of it is that we would keep a memorandum account of the amount of gasoline receipts which Southwestern retained, what the tax rate would be, and also keep a memorandum of account of the tax benefits that could be computed each year as being actually gained by Colorado as a result of this merger, and that you might carry that forward from year to year.

The treatment that I have in mind, which I say as a director I would vote for and as counsel would recommend, is that whenever these figures indicated that a net loss had occurred, that that would not be charged in effect against the ratepayers but the risk of that taken by the stockholders, but that there likewise should be a corresponding credit given to the stockholders whenever the tax benefits were greater.

It might be done in a different way, namely, just carry a balance forward until we could see which way the trend was going, and whenever it got to the point where things seemed to be about balanced off let it go from that time on. That is my reaction to your accounting suggestion and the reasons why I would not agree to it.

Q. This recommendation which you would be willing to make then, as you have stated, would be that the cost of service would be the same after the merger as it would be before the merger?—A. Well, in effect that. That is, here, for example, take on Subexhibit B in Exhibit 38 for the year 1952, where this statement shows that the gasoline receipts to Southwestern, giving effect to a 45 per cent straight income tax, would be $560,817. Now, that amount would be, assuming that it turned out to be that, or whatever amount it might be, carried

in this memorandum account, and then in that year, 1952, there would be computed these tax benefits that were gained to Colorado as a result of this merger.

Now, if these figures would turn out to be as indicated on this exhibit, those benefits show $372,730. So that as of that year there would be, say, $180,000 or $190,000 that would in effect be not included as the cost of service to the consumers.

Now, then, when you get later years where the figure is the other way, those tax benefits should be taken out as not being something that should be given to the consumers, that credit.

I don't know whether I explained myself or not, but that is the way I see it.

Q. I think I understand what you mean. The record will speak for itself.—A. Well, the result I have in mind is that the rate-payers would not be bearing the risk of any loss to this project that might result from giving over this gasoline revenue after credit had been taken for whatever additional tax benefits resulted from the various things that have been discussed.

[Clerk's certificate omitted in printing.]

[fols. 659-660] SUPREME COURT OF THE UNITED STATES

No. 777, OCTOBER TERM, 1953

COLORADO INTERSTATE GAS CO., Petitioner,

vs.

FEDERAL POWER COMMISSION

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI—Filed March 31, 1954

Upon consideration of the application of counsel for petitioner,

It is ordered that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including May 21st, 1954.

Tom C. Clark, Associate Justice of the Supreme Court of the United States.

Dated this 31 day of March, 1954.

[fols. 661-662] (File endorsement omitted.)

[fol. 663] SUPREME COURT OF THE UNITED STATES

No. 710, OCTOBER TERM, 1953

FEDERAL POWER COMMISSION, Petitioner,

vs.

COLORADO INTERSTATE GAS COMPANY

ORDER ALLOWING CERTIORARI—Filed June 7, 1954

The petition herein for a writ of certiorari to the United States Court of Appeals for the Tenth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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APR 23 1954
HAROLD B. WILLEY, Clerk

No. [redacted] 45

In the Supreme Court of the United States

OCTOBER TERM, 1953

FEDERAL POWER COMMISSION, PETITIONER

v.

COLORADO INTERSTATE GAS COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes involved	2
Statement	4
Reasons for granting the writ	9
Conclusion	29

CITATIONS

Cases:

Aircraft & Diesel Corp. v. *Hirsch*, 331 U.S. 752	16
Colorado Interstate Gas Company v. *Federal Power Commission*, 324 U.S. 581	12
Democrat Printing Co. v. *Federal Communications Commission*, 202 F. 2d 298	18
Federal Communications Commission v. *Pottsville Broadcasting Co.*, 309 U.S. 134	13
Federal Power Commission v. *Arkansas Power & Light Co.*, 330 U.S. 802	17
Federal Power Commission v. *Hope Natural Gas Company*, 320 U.S. 591	19
Federal Power Commission v. *Hope Natural Gas Com-* 17	19
Macauley v. *Waterman Steamship Corp.*, 327 U.S. 540	16
Marshall Field & Co. v. *National Labor Relations Board*, 318 U.S. 253	11, 15, 16
May Stores Co. v. *National Labor Relations Board*, 326 U.S. 376	11, 15
National Labor Relations Board v. *Cheney Lumber Co.*, 327 U.S. 385	13, 14
National Labor Relations Board v. *Pinkerton's National Detective Agency*, 202 F. 2d 230	18
National Labor Relations Board v. *Pugh & Barr, Inc.*, 194 F. 2d 217	18
National Labor Relations Board v. *Townsend*, 185 F. 2d 378, certiorari denied, 341 U.S. 909	18
Panhandle Eastern Pipe Line Co. v. *Federal Power Commission*, 324 U.S. 635	12, 14, 15, 16
Switchmen's Union v. *National Mediation Board*, 320 U.S. 297	18
Ries & Co. v. *United States*, 341 U.S. 907	13
Todd v. *Securities & Exchange Commission*, 137 F. 2d 475	16
Unemployment Commission v. *Aragon*, 329 U.S. 143	13, 15
United States v. *Hancock Truck Lines*, 321 U.S. 774	13, 15, 19

Cases—Continued

	Page
United States v. *Northern Pacific R. Co.*, 288 U.S. 490	15
United States v. *Tucker Truck Lines*, 344 U.S. 33	9, 15, 17, 18
United States ex rel. Vajtauer v. *Commissioner*, 273 U.S. 103	15
Wong Yang Sung v. *McGrath*, 339 U.S. 33	18

Statutes:

Administrative Procedure Act, 60 Stat. 237, 5 U.S.C. 1001, *et seq.*):	
Section 10	3-4, 17
Section 10(e)	4, 17
Section 11	16
Civil Aeronautics Act, Section 1006(e), 49 U.S.C. 646(e)	9
Fair Labor Standards Act, Section 10(a), 29 U.S.C. 210(a)	9
Federal Power Act, Section 313(b), 16 U.S.C. 825l(b)	9
National Labor Relations Act, Section 10(e), 29 U.S.C. 160(e)	9
Natural Gas Act, 52 Stat. 821, 15 U.S.C. 717, *et seq.*:	
Section 7	5
Section 19	2
Section 19(a)	3, 11
Section 19(b)	2, 3, 5, 9, 13-14, 16
Public Utility Holding Company, Section 24, 15 U.S.C. 79x	9
Securities Act of 1933, Section 9(a) 15 U.S.C. 77i(a)	9
Securities Exchange Act of 1934, Section 25(a) 15 U.S.C. 78y(a)	9
Trust Indenture Act, Section 322, 15 U.S.C. 77vvv	9

Miscellaneous:

S. Doc. No. 248, 79th Cong. 2d Sess. p. 36	17

In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 710

FEDERAL POWER COMMISSION, PETITIONER

v.

COLORADO INTERSTATE GAS COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

The Solicitor General, on behalf of the Federal Power Commission, prays that a writ of certiorari issue to review that portion of the judgment of the United States Court of Appeals for the Tenth Circuit entered in the above-entitled cause on January 25, 1954, invalidating the condition pursuant to which the Federal Power Commission had excluded from cost of service certain losses from gasoline operations.

OPINIONS BELOW

The original opinion of the Court of Appeals (R. 593-610) is reported at 209 F. 2d 717; its opinion on rehearing (R. 630-633) is reported at 209 F. 2d 732. The opinion and order of the Federal Power Commission directing the rate reduction (R. 77-140) are reported at 95 PUR (NS) 97.[1]

[1] Also pertinent here are the Commission's opinion and order approving the merger of the properties and facilities of Colorado Interstate Gas Company with those of Canadian River Gas Company (R. 549-568). These are reported at 10 FPC 105, 778.

JURISDICTION

The original judgment of the Court of Appeals was entered on October 29, 1953 (R. 610). Pursuant to the Federal Power Commission's timely petition for rehearing, the Court of Appeals on December 8, 1953 vacated its original judgment and granted rehearing (R. 621). The judgment on rehearing was entered on January 25, 1954 (R. 633). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1), and Section 19(b) of the Natural Gas Act (15 U.S.C. 717r (b)).

QUESTION PRESENTED

Whether in a statutory review proceeding of a rate order of the Federal Power Commission, a court has jurisdiction, by reason of asserted inherent power and Section 10(e) of the Administrative Procedure Act, to consider and correct *sua sponte* an alleged error, not raised by the company in the administrative proceeding, in its application for rehearing filed with the Commission, nor in its petition for review, notwithstanding the provision of Section 19(b) of the Natural Gas Act that

> * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

STATUTES INVOLVED

1. Section 19 of the Natural Gas Act (52 Stat. 821, 831, 15 U.S.C. 717r) provides in pertinent part:

(a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. * * * No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

2. Section 10 of the Administrative Procedure Act (60 Stat. 237, 243, 5 U.S.C. 1009) provides in pertinent part:

Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—

* * * * *

(e) SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

STATEMENT

The Federal Power Commission on July 31, 1952, adopted its order directing Colorado Interstate Gas

Company, a "natural-gas company" under the Natural Gas Act, to reduce its rates for sales for resale in interstate commerce by about $2,703,000 a year (R. 77-140). Following the Commission's denial of Colorado's application for rehearing (R. 141-188, 188-204), Colorado filed, as authorized by Section 19(b) of the Natural Gas Act, *supra*, p. 3, a petition for review in the Court of Appeals for the Tenth Circuit, which affirmed the Commission's order in all respects except one (R. 1-9, 593-610). The court in its original opinion held that the Commission had erred in excluding from cost of service a loss of about $420,000 suffered by Colorado on its gasoline operations and remanded the cause to the Commission for further proceedings with respect thereto (R. 601-602). The facts relevant to this issue may be summarized as follows.

Early in 1950, Colorado, jointly with Canadian River Gas Company, requested the Commission to authorize Colorado to acquire and operate all of Canadian's properties pursuant to Section 7 of the Natural Gas Act (R. 564). During the pendency of this application, the question arose as to whether the consumers ultimately receiving gas from Colorado might have to bear an additional expense if at some future time, the expense of certain gasoline plant operations exceeded the proceeds received by Colorado under the merger plan. "To remove this question," Colorado proposed that "in order to keep a rate payer from meeting this deficiency the Commission could condition [its authorization] so as in effect to provide that such deficit would not be considered in determining reasonable rates. In

other words, the stockholders of Colorado * * * would take the risk as to whether or not gasoline prices will go down." (R. 620). Implementing this proposal, Colorado submitted a draft of condition for incorporation into the Commission's order, which, according to Colorado, "would adequately protect ultimate consumers" (R. 620-621). Thereafter, the Commission authorized the merger on the condition, substantially as suggested by Colorado, that (R. 566-567):

> * * * if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pursuant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers.

No review was sought of the Commission's authorization or the condition.

Subsequently, in the rate investigation, the Com-

mission determined that the costs properly allocable to the gasoline operations exceeded the gasoline revenues to Colorado by about $420,000 and, in accordance with the condition excluded this amount from Colorado's cost of service (R. 115). At no time during the rate proceedings did Colorado question the validity of the condition. Although in its application for rehearing Colorado specified about 20 errors in regard to the method used by the Commission in determining the amount of excess costs (R. 148-153, 169-174), it did not question the propriety of excluding the excess costs if properly determined, but on the contrary it assumed that Colorado was required to absorb such costs (R. 171).[2]

In its original opinion the court of appeals rejected Colorado's attack on various aspects of the order, including the Commission's method of determining the excess costs (R. 600-601). However, the court, assuming the question to be before it, went on to rule that the elimination of the excess costs as provided by the condition deprived Colorado of the fair rate of return to which it is entitled and, accordingly, remanded the case to the Commission (R. 601-602, 610).[3]

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[2] As summarized in its petition for review, Colorado urged only that the Commission's method of determining the excess costs was "contrary to the condition imposed upon Petitioner in * * * [the] previous order * * * [and] to all the evidence of record * * *." It admitted that under the terms of the condition Colorado "is to bear" the loss if "'properly' allocable to such operations" (R. 61). See also R. 171-172.

[3] The court's decision requiring that this amount be included in the cost of service, has the additional effect—since the revenues would thereby be increased—of increasing the income tax component of the cost of service. This would

The Commission's petition for rehearing (R. 610-619) pointed out that Colorado had not attacked the validity of the condition in its application for rehearing—or indeed at any other time before the Commission or the court of appeals—and consequently that Section 19(b) of the Act, *supra*, p. 3, precluded consideration thereof by the court. The court granted the rehearing (R. 621), but after further briefing and argument, rejected the Commission's contention (R. 630-633). It held that "it is not correct, as stated by the Commission, to say that Colorado did not object to the exclusion of this item. It did object thereto both in the original proceeding and in its petition for rehearing. It is true, however, that it did not place its objection on the legal ground upon which we predicated our conclusions" (R. 631). In addition, the court ruled that, in any event, it has inherent power in reviewing the Commission's order to consider and correct *sua sponte* manifest and substantial errors; according to the court, Section 19(b) does not deprive it "of its right to consider all relevant matters necessary to determine a just end result" but rather merely means that "one complaining of the order of the Commission will not be heard and has no standing to urge an objection not first submitted to the Commission" (R. 631-632). The court concluded by reading Section 10(e) of the Administrative Procedure Act, *supra*, p. 4, as containing a clear and positive mandate requiring the court *sua*

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result in an over-all increase in the cost of service of $891,902 and so would reduce the rate reduction from about $2,700,000 to about $1,800,000.

sponte to note basic erroneous legal conclusions (R. 632-633).

REASONS FOR GRANTING THE WRIT

The question presented by this case—whether, in the face of a statutory provision which in terms forbids such action, courts may set aside administrative decisions on grounds not presented to the administrative agency—extends beyond the Natural Gas Act and is one of general importance in the delicate area of judicial review of administrative action. A number of statutes providing for review of administrative action—and defining the scope of such review—contain provisions which, like Section 19(b), prohibit judicial consideration of alleged errors by the regulatory body when not raised during the administrative proceeding. See, *e.g.*, Section 313(b) of the Federal Power Act, 16 U.S.C. 825l (b); Section 9(a) of the Securities Act of 1933, 15 U.S.C. 77i(a); Section 322 of the Trust Indenture Act, 15 U.S.C. 77vvv; Section 25(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78y(a); Section 24 of the Public Utility Holding Company Act, 15 U.S.C. 79x; Section 10(a) of the Fair Labor Standards Act, 29 U.S.C. 210(a); Section 10(e) of the National Labor Relations Act, 29 U.S.C. 160(e); Section 1006(e) of the Civil Aeronautics Act, 49 U.S.C. 646(e).[4] Moreover, *United*

[4] While the Natural Gas Act (and the Federal Power Act) preclude judicial consideration of alleged errors not raised by application for rehearing before the Commission, all the other statutes cited in the text require the raising of the alleged error during the administrative proceeding as a condition precedent to its being raised before the reviewing court.

States v. *Tucker Truck Lines*, 344 U.S. 33, suggests that this same rule applies in the absence of such a statutory provision.

1. Even a casual reading of Colorado's assignments of error in its application for rehearing before the Commission (R. 148-153, 169-174) leaves no room for doubt that Colorado was not questioning the validity of the merger condition which the court below struck down. In this application for rehearing, Colorado plainly objected solely to the Commission's method of determining the existence of a loss; Colorado asserted only that the method it proposed rather than that adopted by the Commission, was the proper one, and that under its proposed method, there was no loss to be excluded (*ibid.*) Colorado, thus, raised no question as to the validity of the merger condition itself and indeed, in effect, conceded that the loss, if properly determined, should be excluded from cost of service as required by the condition. Consequently, when the court sustained the Commission's method of determining the loss (R. 600-601), it disposed of the only objection raised by Colorado.

Colorado itself never understood that it questioned—or even that it was in a position to question—the validity of the merger condition. In addition to the fact that it had itself proposed the condition in the merger proceeding in order to obviate an ob-

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Here, Colorado did not question the condition at any time during the rate investigation. See *supra*, p. 7; *infra*, pp. 10-11.

jection to the merger proposed by it (see *supra*, pp. 5-6). Colorado's petition for review filed in the court below in effect admitted that the validity of the condition was not in issue. And in its response to the Commission's petition for rehearing filed in the court below, Colorado conceded (R. 638):

> * * * While Petitioner [Colorado] did not argue the very ground pointed out by the Court for reversal, nevertheless, there was before the Court a record for review of the rate proceeding, and in it was the issue of deducting the Commission found loss on gasoline operations. It can be well understood why Petitioner did not urge as a ground of reversal the ground adopted by the Court. Petitioner having acquiesced in the condition which the Court has struck down could hardly immediately turn its back upon such acquiescence. * * *

While the court below recognized that Colorado had not attacked the validity of the condition as such, it appears to have regarded as sufficient Colorado's objection to the method used by the Commission in determining the loss (R. 631). But it is established that requirements such as that of Section 19(b) may be satisfied only by an "objection * * * sufficiently specific to apprise the [Commission] of the question now presented" (*May Stores Co.* v. *National Labor Relations Board*, 326 U.S. 376, 386, fn. 5; *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U.S. 253, 255), a requirement expressly incorporated in Section 19(a)

of the Gas Act, *supra*, p. 3. Here, there plainly was no such apprisal. Colorado did not object to the exclusion of the loss generally, but rather directed its twenty assignments relative thereto specifically to various aspects of the Commission's method of determining whether there was a loss to be excluded under the condition. These assignments certainly failed to apprise the Commission that the condition itself was under attack. This is especially clear when the assignments are viewed against the condition's prior history, *i.e.*, that the condition had originated in another proceeding at Colorado's behest and that at no time during the rate proceeding had Colorado questioned the condition.

Nor is any different result required because, as the court below asserted "the important and deciding factor in rate hearings is the end result" and "a reviewing court is more concerned with the end result than with the multiple detailed mechanics employed in reaching it." (R. 602). The "end result" of a rate order is not open to court review unless challenged and then only to the extent of such challenge. *Colorado Interstate Gas Company* v. *Federal Power Commission*, 324 U.S. 581, 605-606; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U.S. 635, 649. Here, the "end result" was not challenged because of the exclusion of the loss. Moreover, the "end result" test does not nullify the requirement of specific assignments of error; all it means is that the validity or invalidity of required specific assignments of error are to be examined and passed on in the light

of the impact of the alleged error on the "end result."[5]

2. The court below further committed plain error when it held that even if there had not been compliance with Section 19(b), it nevertheless has inherent power to consider and correct *sua sponte* errors lurking in the record made before the Commission. In so holding, the court failed to distinguish between its functions *vis a vis* the district courts and its functions *vis a vis* administrative agencies. Although the courts of appeals have such inherent power in reviewing judgments of district courts, their jurisdiction over administrative action is far narrower, and is defined by the statutory provisions authorizing review. Cf. *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U.S. 134, 141; *Switchmen's Union* v. *National Mediation Board*, 320 U.S. 297, 300-301; *National Labor Relations Board* v. *Cheney Lumber Co.*, 327 U.S. 385, 388-389; *Unemployment Commission* v. *Aragon*, 329 U.S. 143, 155. And Section

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[5] Colorado's suggestion, that the fact that the validity of the condition was questioned by the Commission staff counsel in the merger proceeding constitutes reasonable excuse for its failure to urge invalidity in the rate proceeding (R. 643, 645), plainly has no substance. It was not Colorado which attacked the condition in the merger proceeding; on the contrary, Colorado there vigorously defended the condition which it itself had proposed. Consequently, the situation presented here is far stronger for preclusion from judicial consideration than if mere failure to raise or even acquiescence were involved. It is established that acquiescence before the administrative agency is sufficient to bar court review without reference to whether the statutory review provision requires raising the issue before the agency. *See United States* v. *Hancock Truck Lines*, 324 U.S. 774, 779-780.

19(b), which vests in the courts of appeals whatever authority they might have to review orders of the Commission, on its face does not permit *sua sponte* consideration of lurking errors. By unambiguously providing that "No objection * * * shall be considered *by the court* * * *" (italics supplied), Section 19(b) patently is not addressed solely at preventing the complaining party from raising new questions, but rather precludes *sua sponte* consideration of such an alleged error by the court as well. Cf. *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U.S. 635, 649.

Moreover, well established principles require that Section 19(b) be read in accordance with its plain language. For example, in *National Labor Relations Board* v. *Cheney Lumber Co.*, 327 U.S. 385, where a court of appeals had struck out a paragraph of a Labor Board order not objected to by the company in the administrative proceeding, this Court reversed, pointing out that the provision in the National Labor Relations Act, comparable to Section 19(b) (see *supra*, p. 9 and fn. 4), constituted "[a] limitation which Congress has placed upon the power of courts to review orders of the Labor Board" (327 U.S. at 388). By this provision "Congress has said in effect that in a proceeding for enforcement of the Board's order the court is to render judgment on consent as to all issues that were contestable before the Board but were in fact not contested * * * [the provision] 'gives emphasis to the salutary policy * * * of

affording the Board opportunity to consider on the merits questions to be urged upon review of its order' " (*id.* at 389). See, also, *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U.S. 253, 255-256; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U.S. 635, 649; *United States* v. *Hancock Truck Lines*, 324 U.S. 774, 779-780; *May Stores Co.* v. *National Labor Relations Board*, 326 U.S. 376, 386, fn. 5; *Unemployment Commission* v. *Aragon*, 329 U.S. 143, 155; *United States* v. *Tucker Truck Lines*, 344 U.S. 33, 36-37; cf. *United States ex rel Vajtauer* v. *Commissioner*, 273 U.S. 103, 113; *United States* v. *Northern Pacific R. Co.* 288 U.S. 490, 494. "[O]rderly procedure and good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts." *United States* v. *Tucker Truck Lines*, *supra*, at 37.[6] Not only the results but the reasoning of these cases foreclose the distinction adopted by the court below that while the complaining party could not raise the issue, the court *sua sponte* could consider it.

Furthermore, contrary to the holding of the court below (R. 632), the salutary rule embodied in Section 19(b) has been applied by this Court

[6] As stated in *Unemployment Commission* v. *Aragon*, 329 U.S. 143, 155:

> A reviewing court usurps the agency's function when it sets aside the administrative determination upon a ground not theretofore presented and deprives the Commission of an opportunity to consider the matter, make its ruling, and state the reasons for its action.

to questions of law as well as issues of fact. Thus even if the "end result" principle be assumed to raise a pure question of law, Section 19(b) nevertheless governs. In the *Marshall Field* case, the question which this Court held could not be considered because not raised before the National Labor Relations Board, related to the Board's power to grant a back pay order which was construed as barring the deduction of unemployment compensation from the award. In the *Panhandle Eastern Pipe Line* case the problem was whether the exemption of Section 1(b) of the Natural Gas Act deprived the Commission of authority to include production and gathering facilities at original cost in the rate base for jurisdictional sales. In the *Tucker Truck Lines* case, the issue concerned the validity of a hearing subject to the Administrative Procedure Act, had before an examiner not appointed pursuant to Section 11 of that Act (5 U.S.C. 1010). See, also, *Todd* v. *Securities and Exchange Commission*, 137 F. 2d 475, 478 (C.A. 6). The issue in each of these cases clearly was not factual in nature, yet the failure to raise it before the administrative agency was held to preclude judicial consideration.[7] Cf. *Macauley* v. *Waterman Steamship Corp.*, 327 U.S. 540, 544;

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[7] Colorado's contention that the rule is inapplicable since the court below "by granting rehearing has afforded" the Commission an "opportunity to present its side of the case on this question" (R. 645), does not bear analysis. Similar "opportunities" in the reviewing court would have been afforded the administrative agency in each of the cases referred to in the text; nevertheless in each case this Court held that the courts were barred from considering the alleged error.

Aircraft & Diesel Corp. v. *Hirsch*, 331 U.S. 752; *Federal Power Commission* v. *Arkansas Power & Light Co.*, 330 U.S. 802.

3. The further holding below that Section 10(e) of the Administrative Procedure Act, *supra*, p. 4, sanctioned such *sua sponte* consideration of issues not raised before the administrative agency, is contrary to the plain language of that Act. Thus, the introductory clause of Section 10 explicitly makes the succeeding subsections inapplicable where "(1) statutes preclude judicial review * * *." This clause, when read with Section 19(b) of the Gas Act, plainly precludes the result reached below. This conclusion is buttressed by the fact that the purpose of the introductory clause was to dovetail the general provisions of the Administrative Procedure Act with the statutory review provisions applicable to particular agencies. See, *e.g.*, S. Doc. No. 248, 79th Cong. 2d Sess. p. 36. Furthermore, while Section 10(e) of the Administrative Procedure Act provides that reviewing courts are to decide "all relevant questions of law * * *," this provision is operative only "where [such questions of law are] presented."

Moreover, this Court has already held that the Administrative Procedure Act does not abrogate the well established principles already discussed. *United States* v. *Tucker Truck Lines*, 344 U.S. 33, was decided several years after the enactment of the Administrative Procedure Act; indeed, it concerned the failure of the Interstate Commerce Commission to comply in its administra[illegible] pro-

ceeding with a requirement of Administrative Procedure Act previously held by this Court to be "jurisdictional." *Riss & Co. v. United States*, 341 U.S. 907; *Wong Yang Sung v. McGrath*, 339 U.S. 33. In there holding that failure to raise the issue before Commission precluded judicial consideration of the alleged error, this Court affirmed the continued vitality of the statutory provisions and judicial decisions relating to the necessity of raising issues before administrative agencies before they may be considered by the reviewing courts. 341 U.S. at 36-37; see, also, *National Labor Relations Board v. Townsend*, 185 F. 2d 378, 380-381 (C.A. 9), certiorari denied, 341 U.S. 909; *National Labor Relations Board v. Pinkerton's National Detective Agency*, 202 F. 2d 230, 233 (C.A. 9); *National Labor Relations Board v. Pugh & Barr, Inc.*, 194 F. 2d 217, 220 (C.A. 4); *Democrat Printing Co. v. Federal Communications Commission*, 202 F. 2d 298, 303-304 (C.A. D.C.).

4. Finally, it should be noted that, as already indicated, the provision as to the exclusion of excess costs was incorporated in a condition imposed by the Commission in approving Colorado's application for authority to merge with Canadian River Gas Company in another proceeding. The condition was suggested by Colorado to eliminate an objection to the proposed merger and was an important element relied on by the Commission in reaching its conclusion that the merger would be in the public interest. Colorado itself would have been estopped from challenging the condition in

which it had more than acquiesced. *United States* v. *Hancock Truck Lines*, 324 U. S. 771, 779, 780. The effect of the court's ruling here is not only to strike down the condition in a collateral proceeding but to leave the merger outstanding without the condition. Since the determination whether the merger would be consistent with the public interest without the condition is one to be made by the Commission, the court's action infringes upon the administrative function, in violation of the long-settled principle most recently reiterated in *Federal Power Commission* v. *Idaho Power Co.*, 344 U. S. 17.*

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* The exclusion of the loss from cost of service represented an appropriate "balancing of the investor and the consumer interests" by the Commission (*Federal Power Commission* v. *Hope Natural Gas Company*, 320 U. S. 591, 603) and did not impair the financial integrity or credit of Colorado. During the pendency of the rate proceedings, there was a public offering of Colorado's common stock with full disclosure to prospective investors that the loss under the merger condition would not be "considered as a cost of service to Colorado's natural-gas consumers," but would be borne by the investors. (Tr. 2685, 2694). Notwithstanding this, the common stock was promptly over-subscribed. As the court of appeals noted in sustaining the Commission's finding that 5¾% is a fair rate of return (R. 608):

> The fact that this offering was promptly oversubscribed is evidence of the standing of Colorado with the investing public and, if we must as urged by Colorado take into account that the eagerness to purchase this stock was motivated in the belief of the future development of Colorado's resources, we must on the other hand not be unmindful that that manifested interest was in the face of a rate hearing which might well, as it did, result in a decrease of rates.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted. Moreover, since the decision below is so clearly contrary to the consistent rulings of this Court on the point in question, the Court might appropriately consider reversing the judgment of the court below without further briefs or argument.

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APRIL, 1954.

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In the Supreme Court of the United States

OCTOBER TERM, 1954

FEDERAL POWER COMMISSION, PETITIONER

v.

COLORADO INTERSTATE GAS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

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INDEX

	Page
Opinions below	1
Jurisdiction	2
Question presented	2
Statutes involved	3
Statement	3
Summary of argument	6
Argument:	
The court of appeals lacked authority to consider the validity of the merger condition	12
A. Colorado did not question the validity of the merger condition in the rate proceedings or in its application for rehearing before the Commission and the issue is therefore precluded by Section 19(b) of the Gas Act from consideration in the court of appeals	14
B. The court of appeals had no inherent power to consider the condition's validity in the absence of compliance with Section 19(b) of the Gas Act	25
C. The Administrative Procedure Act does not do away with the necessity of compliance with Section 19(b)	40
D. The court of appeals erroneously exercised an administrative function in invalidating the condition on which the Commission had predicated its approval of the merger	48
Conclusion	55
Appendix	56

CITATIONS

Cases:

Addison v. Holly Hill Co., 322 U. S. 607	49
Aircraft & Diesel Corp. v. Hirsch, 331 U. S. 752	32, 38
Allen v. Grand Central Aircraft Co., 347 U. S. 535	41

Cases—Continued

	Page
Blackmar v. *Guerre*, Oct. Term, 1951, No. 361 (Government brief)	45
Booth Fisheries v. *Industrial Commission*, 271 U.S. 208	23
Buck v. *Kuykendall*, 267 U.S. 307	23
Callanan Road Co. v. *United States*, 345 U.S. 507	23
Colorado Interstate Gas Company v. *Federal Power Commission*, 324 U.S. 581	24
Daniels v. *Tearney*, 102 U.S. 415	23
Democrat Printing Co. v. *Federal Communications Commission*, 202 F. 2d 298	43
Fahey v. *Mallonee*, 332 U.S. 245	23
Far East Conference v. *United States*, 342 U.S. 570	49
Federal Communications Commission v. *Pottsville Broadcasting Co.*, 309 U.S. 134	26, 49
Federal Power Commission v. *Arkansas Power & Light Co.*, 330 U.S. 802	32
Federal Power Commission v. *Hope Natural Gas Co.*, 320 U.S. 591	24, 28, 33, 36
Federal Power Commission v. *Idaho Power Co.*, 344 U.S. 17	11, 49, 54
Federal Power Commission v. *Natural Gas Pipeline Co.*, 315 U.S. 575	34
Federal Power Commission v. *Pacific Power & Light Co.*, 307 U.S. 156	26, 53
Federal Trade Commission v. *Morton Salt Co.*, 334 U.S. 37	49
Federal Trade Commission v. *Royal Milling Co.*, 288 U.S. 212	49
Ford Motor Company v. *National Labor Relations Board*, 305 U.S. 364	49
Franklin v. *Jonco Aircraft Corp.*, 346 U.S. 868	44
Grand Rapids and Indiana Railway Co. v. *Osborn*, 193 U.S. 17	23
Gray v. *Powell*, 314 U.S. 402	38
Halsted v. *Securities Exchange Commission*, 182 F. 2d 660	42
Heikkila v. *Barber*, 345 U.S. 229	45

Cases—Continued

	Page
Helvering v. *Wood*, 309 U.S. 344	23, 53
Hornel v. *Helvering*, 312 U.S. 552	29
Johnson v. *Shaughnessy*, 336 U.S. 806	46
Louisville Gas & Electric Co. v. *Federal Power Commission*, 129 F. 2d 126	53
Macauley v. *Waterman Steamship Corp.*, 327 U.S. 540	32
Marshall Field & Co. v. *National Labor Relations Board*, 318 U.S. 253	7, 18, 20, 28, 32
Martinez v. *Neelly*, Oct. Term, 1952, No. 218 (Government brief)	45
May Stores Co. v. *National Labor Relations Board*, 326 U.S. 376	18, 29, 28, 29
Miles Laboratories v. *Federal Trade Commission*, 140 F. 2d 683, certiorari denied, 322 U.S. 752	53
National Labor Relations Board v. *Auburn Curtain Co.*, 193 F. 2d 826	42, 45
National Labor Relations Board v. *Bradford Dyeing Ass'n*, 310 U.S. 318	28
National Labor Relations Board v. *Cheney Lumber Co.*, 327 U.S. 385	8, 9, 26, 27, 30, 31, 33
National Labor Relations Board v. *G. W. Thomas Drayage & Rig. Co.*, 206 F. 2d 857	36, 43
National Labor Relations Board v. *Jones & Laughlin Co.*, 331 U.S. 416	29
National Labor Relations Board v. *Kinner Motors*, 154 F. 2d 1007, modifying 152 F. 2d 816	31
National Labor Relations Board v. *Norman*, 193 F 2d 172	42
National Labor Relations Board v. *Pappas & Co.*, 203 F. 2d 569	43
National Labor Relations Board v. *Pinkerton's National Detective Agency*, 202 F. 2d 250	42
National Labor Relations Board v. *Pugh & Barr, Inc.*, 194 F. 2d 217	42
National Labor Relations Board v. *Sewell p Co.*, 344 U.S. 344	19, 20, 28, 30, 33, 41
National Labor Relations Board v. *Townsend*, 185 F. 2d 378, certiorari denied, 341 U.S. 909	42

Cases—Continued

Page

National Labor Relations Board v. *Van De Kamp's Holland-Dutch Bakeries, Inc.*, 154 F. 2d 828, modifying 152 F. 2d 818 31

Panhandle Eastern Pipe Line Co. v. *Federal Power Commission*, 324 U.S. 635 ..... 24, 25, 27, 28, 29

Pittsburgh Steamship Co. v. *National Labor Relations Board*, 180 F. 2d 731, affirmed, 340 U.S. 498 46

Riss & Co. v. *United States*, 341 U.S. 907 41

Rochester Telephone Corp. v. *United States*, 307 U.S. 125 38

Shepard v. *Barron*, 194 U.S. 553 23

Shields v. *Utah Idaho Central R.R.*, 305 U.S. 177 .. 38

Siegel Co. v. *Federal Trade Commission*, 327 U.S. 608 49

Southern Ry. Co. v. *Tift*, 206 U.S. 428 49

Stark v. *Wickard*, 321 U.S. 288 26

St. Louis, Brownsville & Mexico Ry. Co. v. *Brownsville Navigation District*, 304 U.S. 295 49

St. Louis Malleable Casting Co. v. *George C. Prendergast Construction Co.*, 260 U.S. 469 23

Switchmen's Union v. *National Mediation Board*, 320 U.S. 297 26

Tank Car Corporation v. *El Dorado Terminal Co.*, 308 U.S. 422 49

Texas & Pac. Ry. v. *Abilene Cotton Oil Co.*, 204 U.S. 426 49

Todd v. *Securities and Exchange Commission*, 137 F. 2d 475 36

Unemployment Compensation Commission v. *Aragon*, 329 U.S. 143 ..... 26, 28, 31, 33, 37, 38

United Fuel Gas Co. v. *Railroad Commission*, 278 U.S. 300 23

United States v. *Atkinson*, 297 U.S. 157 26

United States v. *Capital Transit Co.*, 338 U.S. 286 ..... 24, 28, 35, 41

United States v. *Hancock Truck Lines*, 324 U.S. 774 ..... 8, 23, 28, 37, 53

United States v. *Northern Pacific R. Co.*, 288 U.S. 490 ..... 28, 37

Cases—Continued

Page

United States v. *Ruzicka*, 329 U.S. 287 34
United States v. *San Francisco*, 310 U.S. 16 23
United States v. *Tucker Truck Lines*, 344 U.S. 33 ..... 9, 10, 23, 28, 31, 32, 37, 41
United States ex rel. Beck v. *Neelly*, 202 F. 2d 221 42
United States ex rel. Vajtauer v. *Commissioner*, 273 U.S. 103 ..... 28, 37
Universal Camera Corp. v. *National Labor Relations Board*, 340 U.S. 474 ..... 26, 46
Wall v. *Parrot Silver & Copper Co.*, 244 U.S. 407 .. 23
West Ohio Gas Co. v. *Public Utilities Commission*, 294 U.S. 63 34
West Texas Utilities Co. v. *National Labor Relations Board*, 184 F. 2d 233 42
Wong Yang Sung v. *McGrath*, 339 U.S. 33 41
Woods v. *Kaye*, 175 F. 2d 886 53

Statutes:

Administrative Procedure Act, 60 Stat. 237, 5 U.S.C. 1001, *et seq.*:

Section 5(c) 43
Section 7(c) 45
Section 8(b) 45
Section 10 10
Section 10(b) 45, 58
Section 10(c) 11, 59
Section 10(e) 2, 10, 13, 44, 59
Section 11 ..... 32, 41

Civil Aeronautics Act, 49 U.S.C. 646(c):

Section 1006(c) 21

Fair Labor Standards Act, 29 U.S.C. 210(a):

Section 10(a) 21

Federal Power Act, 16 U.S.C. 825*l*(b):

Section 313(b) 21

Statutes—Continued

Page

National Labor Relations Act, 29 U.S.C. 160(c):

Section 10(c) 21

Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717, *et seq.*:

Section 1(b) 32
Section 7 ..... 4, 52
Section 7(c) 56
Section 7(e) 11, 50, 56
Section 19(a) 19, 57
Section 19(b) 2, 7, 9, 12, 13, 14, 26, 31, 57

Public Utility Holding Company Act, 15 U.S.C. 79x:

Section 24 21

Securities Act of 1933, 15 U.S.C. 77i(a):

Section 9(a) 21

Securities Exchange Act of 1934, 15 U.S.C. 78y(a):

Section 25(a) 21

Trust Indenture Act, 15 U.S.C. 77vvv:

Section 322 21
28 U.S.C. 2321-2325 37

Miscellaneous:

H. Rep. No. 1980, 79th Cong., 2d Sess., p. 47 43

S. Doc. 248, 79th Cong., 2d Sess. (Legislative history of the Administrative Act):

pp. 229-230 ..... 11, 48
p. 281 43
p. 289 ..... 11, 47
p. 307 48
p. 311 ..... 11, 47
p. 369 48
p. 374 ..... 11, 48

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION

OPINIONS BELOW

The original opinion of the Court of Appeals (R. 262-279) is reported at 209 F. 2d 717; its opinion on rehearing (R. 299-302) is reported at 209 F. 2d 732. The opinion and order of the Federal Power Commission directing the rate reduction (R. 47-97) are reported at 95 PUR (NS) 97.[1]

[1] Also pertinent here are the Commission's opinion and order approving the merger of the properties and facilities of Colorado Interstate Gas Company with those of Canadian River Gas Company (R. 243-261). These are reported at 10 FPC 105, 778.

JURISDICTION

The original judgment of the Court of Appeals was entered on October 29, 1953 (R. 279). Pursuant to the Federal Power Commission's timely petition for rehearing, the Court of Appeals on December 8, 1953, vacated its original judgment and granted rehearing (R. 290). The judgment on rehearing was entered on January 25, 1954 (R. 302). The petition for a writ of certiorari was filed on April 23, 1954, and granted on June 7, 1954 (R. 327). 347 U.S. 1009. The jurisdiction of this Court rests upon 28 U. S. C. 1254(1), and Section 19(b) of the Natural Gas Act (15 U. S. C. 717r (b)).

QUESTION PRESENTED

Whether, in a statutory review proceeding of a rate order of the Federal Power Commission, a court of appeals has jurisdiction, by reason of asserted inherent power and Section 10(e) of the Administrative Procedure Act, to consider and correct *sua sponte* an alleged error not raised by the company in the administrative proceeding, in its application for rehearing filed with the Commission, or in its petition for review notwithstanding the provision of Section 19(b) of the Natural Gas Act that:

> * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

STATUTES INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U. S. C. 717 *et seq.*, and of the Administrative Procedure Act, 60 Stat. 237, 5 U. S. C. 1001, *et seq.*, are set forth in the Appendix, *infra*, pp. 56-60.

STATEMENT

The Federal Power Commission, on July 31, 1952, adopted an order directing Colorado Interstate Gas Company, a "natural-gas company" under the Natural Gas Act, to reduce its rates for sales for resale in interstate commerce by about $2,730,000 a year (R. 47-97).[2] Following the Commission's denial of Colorado's application for rehearing (R. 118-130), Colorado filed, as authorized by Section 19(b) of the Natural Gas Act, *infra*, pp. 57-58, a petition for review in the Court of Appeals for the Tenth Circuit, which affirmed the Commission's order in all respects except one (R. 262-279). In its original opinion, the court held that the Commission had erred in excluding from cost of service a loss of about $420,000 suffered by Colorado on its gasoline operations and remanded the cause to the

[2] While the Commission ordered a rate reduction in the gross amount of about $3,100,000 (R. 96), the Commission also found that the revenues received by Colorado from its sale to Natural Gas Pipeline Company did not meet the cost of service by about $380,000 (R. 94). Since the Commission could not make the appropriate rate increase without application therefor by the company, the Commission suggested that Colorado take the initiative (R. 94). With this rate increased, as it was, the net amount of the rate reduction became $2,730,000, as set out in the text.

Commission for further proceedings with respect thereto (R. 279). The facts relevant to this issue may be summarized as follows:

Early in 1950, Colorado, jointly with Canadian River Gas Company, requested the Commission to authorize Colorado to acquire and operate all of Canadian's properties pursuant to Section 7 of the Natural Gas Act, *infra*, pp. 56-57, (R. 243-261). During the Commission's consideration of this application, the question arose as to whether the consumers ultimately receiving gas from Colorado might have to bear an additional expense if, at some future time, the cost of certain gasoline plant operations exceeded the revenues received therefrom by Colorado under the merger plan. "To remove this question", Colorado proposed in a letter to the Commission dated June 8, 1950, that "in order to keep a rate payer from meeting this deficiency the Commission could condition [its authorization] so as in effect to provide that such deficit would not be considered in determining reasonable rates. In other words, the stockholders of Colorado * * * would take the risk as to whether or not gasoline prices will go down." (R. 289). Implementing this proposal, Colorado simultaneously submitted for incorporation into the Commission's order, approving the merger, a draft of condition which, according to Colorado, "would adequately protect ultimate consumers" (R. 289).

Thereafter, the Commission approved the merger on the condition, substantially as suggested to it by Colorado, that (R. 260):

> * * * if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pursuant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers.

No review was sought by Colorado of the Commission's approval or of the condition.

Subsequently, in the rate investigation, the Commission determined that the costs properly allocable to the gasoline operations exceeded the gasoline revenues received by Colorado by about $420,000 (R. 79). In accordance with the terms of the condition, the Commission excluded this amount from Colorado's cost of service (R. 79).

In its original opinion, the Court of Appeals rejected Colorado's attack on various aspects of the

order, including the method by which the Commission had determined that the costs of the gasoline operations exceeded the revenues received therefrom (R. 262-279). However, the court, assuming the question to be before it, went on to rule that the exclusion of the excess costs from Colorado's cost of service, in accordance with the terms of the condition, resulted in denying to Colorado the fair rate of return to which it is entitled and, accordingly, remanded the case to the Commission (R. 279).[3]

The Commission petitioned for rehearing, urging that since Colorado had failed to raise the question during the administrative proceeding and particularly in its petition for rehearing before the Commission, Section 19(b) *infra*, p. 58 precluded the court from considering the issue (R. 280-283). The court granted rehearing to the Commission (R. 290) but, after further briefing and argument, the court adhered to its original position and remanded the case to the Commission for further proceedings in accordance with its original opinion (R. 299-302).

SUMMARY OF ARGUMENT

There is no merit to any of the grounds on which the Court of Appeals based its exercise of jurisdic-

[3] The court's decision, requiring that this amount be included in the cost of service, has the additional effect—since the revenues would thereby be increased—of increasing the federal and state income tax components of the cost of service by $436,065 and $43,709, respectively. This, together with the $120,000 excess costs, would result in an over-all increase in the cost of service of about $892,000, and so would reduce the net rate reduction from about $2,700,000 to about $1,808,000.

tion in this rate case to invalidate the condition of the merger proceeding pursuant to which the Commission excluded Colorado's gasoline losses from the cost of operation.

A.

Colorado did not question the validity of the condition in its application for rehearing before the Commission, as specifically required by Section 19(b) of the Natural Gas Act.[1] The several specifications dealing directly with the gasoline loss were all concerned with the Commission's method of determining the existence and amount of the loss, but not to the exclusion of the loss if properly determined. Indeed, Colorado conceded that the loss, if properly determined, should be excluded as required by the condition, a position from which Colorado did not depart at any time during the rate investigation and in the proceedings in the court below, up to its response to the Commission's petition for rehearing (R. 306). In these circumstances, the assignments of error so addressed were plainly not sufficiently specific to apprize the Commission that the exclusion of the loss was itself at issue (see *e.g.*, *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U.S. 253, 255), particularly since Colorado, in the merger proceeding, had proposed the condition to the Commission in order to over-

[1] "* * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *"

come an obstacle to Commission approval of the merger, and expressed confidence in its legality in the teeth of objections by the Commission's staff. Since Colorado more than acquiesced in the condition, the situation here is far stronger for preclusion of the issue from judicial consideration than the mere acquiescence involved in *United States v. Hancock Truck Lines*, 324 U.S. 774, 779-780. Nor does the "end-result" test, applicable in review of rate orders, make Section 19(b) inoperative or permit a summary objection to the "end-result" to substitute for specific assignments addressed to specific points; the "end-result" rule merely provides the general test in the light of which to examine the specific assignments.

B.

The court below also erred in holding that it has inherent power *sua sponte* to consider and correct alleged errors lurking in the record. Unlike their relation to District Courts, Courts of Appeals have jurisdiction over administrative action only to the extent provided in the pertinent statutory provision. And here Section 19(b) unequivocally precludes judicial consideration of issues not preserved in an application for rehearing to the Commission, a provision, which it is settled, is to be read in accordance with its plain language. *See e.g., National Labor Relations Board v. Cheney Lumber Co.*, 327 U.S. 385, 388-389. The strength of the rule is indicated by this Court's insistence upon compliance with provisions like Section

19(b) even where failure to comply was not pressed by the agency (*e.g.*, *Cheney Lumber case*, *supra*); the Court has applied the rule even in the absence of a special statutory requirement (*e.g.*, *United States* v. *Tucker Truck Lines*, 344 U.S. 33, 36-37).

The attempted distinction that Section 19(b) applies only to issues of fact, and the question here is one of law, cannot stand. The evalution of the financial data necessary to ascertain the reasonableness of the Commission's rate order—or of the merger condition—can hardly be considered a pure question of law. And even if it were, the settled law requires the raising of such issues, and indeed even of constitutional issues, before the administrative agency, if there is later to be judicial consideration of the question.

To sanction judicial invalidation of the merger condition—after Colorado had affirmatively proposed the condition to obtain Commission approval of the merger and had left it wholly unchallenged during the rate investigation—would be contrary to the considerations underlying the requirement embodied in Section 19(b), as well as the closely related doctrine of exhaustion of administrative remedies. For, by upsetting the condition, the court below made a completely *de novo* examination of the issue, without the benefit of analysis by the experienced agency, without reference to the limitations on review of administrative determinations, and on the basis of a record made in another proceeding and not addressed to this issue. In addition to usurping administrative functions, the

court's action thus threatens the orderly functioning of the administrative process.

C.

Section 10 ("Judicial Review") of the Administrative Procedure Act does not do away with the necessity of raising issues before the administrative agency as required by Section 19(b) of the Gas Act. Since the enactment of the Procedure Act in June 1946, this Court has in several decisions recognized the continued vitality of the requirement and reaffirmed the pre-Administrative Procedure Act decisions. See, particularly, *United States* v. *Tucker Truck Lines*, 344 U.S. 33, applying the rule where a motor carrier had failed during the administrative proceedings to raise the agency's omission to comply with the Administrative Procedure Act. The courts of appeals have repeatedly assumed that issues not raised before the administrative agency are still precluded from judicial consideration and this Court has continued to recognize the continued vitality of the closely-related doctrine of exhaustion of administrative remedies.

The provision of Section 10(e) relied on by the court below,[3] when read together with other parts of Section 10, does not have the scope attributed to it. In addition to the overriding clause which makes the Section's provisions inapplicable where

[3] "So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. * * *"

"statutes preclude judicial review," other subsections, particularly Section 10(e), indicate no purpose to change the law on this issue, and even the language relied on by the court is subject to the limitation "where presented." In addition, the legislative history on several occasions reveals a general intention not to depart from the past in this type of matter. See, *e.g.*, S. Doc. No. 248, 79th Cong., 2d Sess., p. 289, fn. 21, 311, 369, 374, 229-230.

D.

In invalidating the condition on which the Commission had predicated its approval of the merger, the court below also erred in improperly undertaking to exercise an administrative function. Section 7(e) of the Gas Act authorizes the Commission to approve mergers, and to subject them to such conditions as it finds to be in the public interest. Moreover, it is extremely doubtful whether the Commission would have approved the merger without the condition which Colorado represented would adequately protect ultimate consumers (R. 289). To strike down the condition in these circumstances, while permitting the merger itself to remain in effect, was plainly incorrect under long established principles most recently reiterated in *Federal Power Commission* v. *Idaho Power Co.*, 344 U. S. 17, 20-21. The condition was an integral element of the Commission's approval of the merger, and, if Colorado were not estopped, immediate and direct review of the condition would have been available in the merger proceeding. If Colorado would have been estopped to challenge the

condition on review of the merger order—as we believe it would have been—that is all the more reason for holding the matter likewise foreclosed in the rate proceeding.

ARGUMENT

The Court of Appeals Lacked Authority to Consider the Validity of the Merger Condition

In its original judgment, the Court of Appeals reversed the Commission's order directing Colorado to reduce its rates by at least $2,700,000 on the ground that the condition forming a basis of the Commission's approval, in another proceeding, of the merger of Colorado's properties with those of Canadian River Gas Company was invalid and, consequently, that the Commission erred in excluding, in accordance with this condition, the $420,000 gasoline loss from Colorado's cost of service. On rehearing, the Commission pointed out that under the terms of Section 19(b) of the Natural Gas Act, *infra*, p. 58, the court lacked jurisdiction to pass on the validity of the condition since at no time during the rate proceedings, either before the Commission or the court, had Colorado attacked the validity of the condition—and, indeed, it had suggested and affirmatively pressed adoption of the condition in the merger proceeding.

Nevertheless, the court below reentered its judgment reversing the Commission's order. Its opinion on rehearing based its exercise of jurisdiction on three grounds. First, it held that "it is not correct, as stated by the Commission, to say that

Colorado did not object to the exclusion of this item. It did object thereto both in the original proceeding and in its petition for rehearing. It is true, however, that it did not place its objection on the legal ground upon which we predicated our conclusions" (R. 300). Second, the court ruled that, in any event, it has inherent power in reviewing the Commission's order to consider and correct *sua sponte* manifest and substantial errors; according to the court, Section 19(b) does not deprive it "of its right to consider all relevant matters necessary to determine a just end result" but rather merely means that "one complaining of the order of the Commission will not be heard and has no standing to urge an objection not first submitted to the Commission" (R. 300). The court concluded by reading Section 10(e) of the Administrative Procedure Act, *infra*, pp. 59-60, as containing a clear and positive mandate requiring it *sua sponte* to note basic legal conclusions which were erroneous (R. 301-302).

Each of these grounds, we submit, is devoid of merit. In our view, Section 19(b) completely bars consideration by the reviewing court of the validity of the condition.

A. COLORADO DID NOT QUESTION THE VALIDITY OF THE MERGER CONDITION IN THE RATE PROCEEDINGS OR IN ITS APPLICATION FOR REHEARING BEFORE THE COMMISSION AND THE ISSUE IS THEREFORE PRECLUDED BY SECTION 19(b) OF THE GAS ACT FROM CONSIDERATION IN THE COURT OF APPEALS

1. The record shows that *at no time* during the rate investigation before the Commission—or during the merger proceeding in which Colorado proposed the condition to the Commission—did Colorado raise any question as to the validity of the merger condition which the Court of Appeals struck down. But in view of the express provision of Section 19(b) (*infra*, p. 58) prohibiting courts from considering objections to orders of the Commission "unless such objection shall have been urged before the Commission *in the application for rehearing*" (emphasis added), we first discuss whether Colorado questioned the condition in its application for rehearing before the Commission.

Even a casual reading of that application leaves no doubt that Colorado did not in the document raise any question as to the validity of the condition. Colorado sets out seventeen errors allegedly committed by the Commission in connection with the exclusion of the loss resulting from gasoline operations. The pertinent specifications (Specifications 20 through 36) are reproduced in full at R. 98-103; they are aptly summarized in Specification 20 which reads (R. 98-99):

> The Commission erred in concluding that Colorado would experience a loss in gasoline

> operations since it has presumed to follow a theory which is not based upon the substantial evidence of record, which is based upon data missing from the record, and which is contrary to all of the substantial evidence of this record.

Specifications such as these are plainly directed at the method used by the Commission in ascertaining the existence and amount of the loss and not at the condition under which the Commission excluded the loss thus determined from the cost of service. Colorado was contending only that there was a net profit, not a loss, from these gasoline operations (See R. 269); it did not urge that if the method used by the Commission in ascertaining the loss was proper, that loss should be treated otherwise than as provided in the condition.

That Colorado was attacking the method by which the loss was ascertained and not the validity of the exclusion, once it was determined that the loss was properly ascertained, is further apparent from the argumentative discussion of these specifications in the application for rehearing under the caption "Grounds Relied Upon." (R. 104). The discussion bearing on these specifications opens with the statement (R. 106):

> The Commission in its adoption of one of the two methods of costing gasoline which it held to be unsatisfactory has purported to adopt the relative market value method proposed by the Staff.

Later, in its discussion, Colorado urged (R. 109):

> The Commission here under the justification of the condition in its order in the merger case has assumed to attribute costs to gasoline operations. The merger case condition required Colorado to absorb costs in excess of revenues accruing to it, but as the order in that case expressly recites it is only "the costs properly allocable to such hydrocarbons" which are to be considered in imposing such liability. The Commission cannot determine the costs properly allocable to the hydrocarbons without having before it a thoroughly satisfactory method of cost determination. The Staff, therefore, failed in its burden of proof in this regard and there is no substantial evidence upon which the Commission could act.

And Colorado concluded the discussion with a statement of its affirmative position (R. 112):

> The volumetric method is the only appropriate method here since (i) it accords with the facts—volume determines size of facilities; (ii) it accords with the Commission's method of allocating other costs; and (iii) this is the only method supported by the qualified expert witnesses in this case.

It is thus entirely clear that Colorado's application for rehearing did not question the validity of the merger condition itself. On the contrary, Colorado conceded that the gasoline operation loss, if properly determined, should be excluded from cost of service as required by the condition. Accord-

ingly, when the court below sustained the Commission's method of determining the loss (R. 270), it disposed of the only objections in regard to the gasoline loss which had been raised in Colorado's application for rehearing."

Moreover, the simple fact is that, prior to the original opinion of the court below, Colorado never understood at any time that it had questioned—or even that it was in a position to question—the legality of the merger condition. It had itself proposed the condition to the Commission in the merger proceeding in order to eliminate, if possible, an objection to the merger proposed by it (see *supra*, pp. 4-5; *infra*, pp. 21-23, 51-52). Its petition for review filed in the court below (R. 1-9) in effect admitted that the validity of the condition was not—and had not been—in issue. As summarized in this petition, Colorado visualized its contention as being only that the Commission's method of determining the gasoline operation loss was "contrary to the condition imposed upon [Colorado] in * * * [the] previous order * * *" (R. 7). At the

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[6] Colorado appears to suggest in its brief in opposition to certiorari (see *e.g.*, pp. 6, 7, 10-11 and fn. 6) that the issue was raised by the specifications in regard to the tax adjustment resulting from the exclusion of the loss (see *supra*, p. 6, fn. 3). But the specification of error relating to taxes (Specification 40, R. 103), and the pertinent discussion in the application for rehearing (R. 112), obviously have no bearing on the merger condition's validity. Moreover, the discussion in the Commission's opinion on rehearing on this specification, set out in Colorado's brief in opposition, pp. 10-11, fn. 6 (see also R. 127), clearly reveals that the Commission did not understand the specification in regard to income taxes as in any way touching the validity of the merger condition itself.

same time that it made this claim, Colorado expressly recognized in its petition for review that "under the terms of a previous order entered by the Commission [Colorado] is to bear [the loss] if such loss is 'properly' allocable to such operations" (R. 7). Even after the court's original opinion, Colorado still conceded in its response to the Commission's petition for rehearing (R. 306):

> While [Colorado] did not argue the very ground pointed out by the Court for reversal, nevertheless, there was before the Court a record for review of the rate proceeding, and in it was the issue of deducting the Commission found loss on gasoline operations. *It can be well understood why Petitioner did not argue as a ground of reversal the ground adopted by the Court. Petitioner having acquiesced in the condition which the Court has struck down could hardly immediately turn its back upon such acquiescence.* * * * (emphasis added.)

2. Although the Court of Appeals admitted that Colorado had not attacked the validity of the condition as such, *i. e.*, "the legal ground upon which we predicated our conclusions" (R. 300), it appears to have regarded Colorado's objection to the method used by the Commission in determining the loss as sufficient to give authority to consider the question (R. 300). But it is established that requirements such as that of Section 19(b) may be satisfied only by an "objection * * * sufficiently specific to apprise the [Commission] of the question now presented" (*May Stores Co.* v. *National Labor Re-*

stant to the merger condition, was proper (if considered alone). This involves consideration of the facts and circumstances surrounding the imposition of the condition, especially the fact that Colorado's counsel proposed the condition to the Commission.[7] Nor can it be concluded as a matter of law, as the court below said, that "[A] rate based upon the exclusion from the cost of service, *no matter for what reason*, of a substantial amount of admitted operative cost does not and cannot result a just and reasonable result and may, therefore, not stand" (R. 271). The court cannot shut its eyes to the facts, reasons, and circumstances surrounding the exclusion and conclude that there is presented only a bare question of law which can be decided apart from a proper inquiry into the facts and proper administrative findings. Cf. *Federal Power Commission* v. *Natural Gas Pipeline Company*, 315 U. S. 575; *West Ohio Gas Company* v.

[7] In *United States* v. *Rock Royal*, 329 U. S. 287, 294, the contention was made in an enforcement proceeding under the Agricultural Marketing Agreement Act that the order sought to be enforced was not "in accordance with law." The court disposed of this contention by the statement that:

> The short answer to this rather dialectic point is that whether such an order is or is not in accordance with law is not a question that brings its own immediate answer, or even an answer which it is the familiar everyday business of courts to find. Congress has provided a special procedure for ascertaining whether such an order is or is not in accordance with law. The questions are not or may not be abstract questions of law. Even when they are formulated in constitutional terms they are questions of fact arising out of, or entangled with, factors that call for understanding of the milk industry.

lations Board, 326 U. S. 376, 386, fn. 5; *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U. S. 253, 255; *National Labor Relations Board* v. *Seven-Up Co.*, 344 U. S. 344, 350), a requirement expressly incorporated in Section 19(a) of the Gas Act.[7]

Here, the Company's objections plainly did not give the Commission notice that the legality of the condition was in issue. This is not surprising since, as we have pointed out, the Company did not intend to present this issue and did not think that it was doing so. Colorado did not object to the exclusion of the loss if properly determined, but rather directed its numerous assignments on this matter to various specific aspects of the Commission's method of determining the existence of a loss and the amount thereof. Once the loss was properly determined, everybody, including Colorado, accepted during the rate investigation the proposition that the excess costs were to be excluded by virtue of the condition. The assignments of error, addressed as they were to an entirely different problem than the condition's validity, certainly failed to apprise the Commission that the condition itself was under attack. This is especially clear when the assignments are viewed against the condition's prior history—it had originated in another proceeding, proposed to the Commission by Colorado to allay an objection which if not overcome would probably have resulted in the Commission's

[7] Section 19(a) requires that "the application for rehearing shall set forth specifically the ground or grounds upon which such application is based." See *infra*, p. 57.

Public Utilities Commission, 294 U.S. 63.[18] For this reason (among others), the court erred in concluding that it is no "answer to say that this was a condition of the merger order and that, therefore, Colorado's stockholders are bound and saddled with this loss. We are dealing here with a business affected with a public interest. Parties in such businesses are not free to contract as they choose" (R. 271). If this means that the freedom of choice on the part of natural-gas companies is limited to reasonable and prudent operation, a finding of reasonableness or unreasonableness would necessarily depend on the whole record of the merger proceeding, as well as on findings as to the company's whole business, factors which were not before the Court of Appeals nor are they before this Court. See also *supra*, p. 33; *infra*, pp. 39-40 and fn. 19.

(c) That the precluded issue may be a constitutional one does not affect the application of Section 19(b), which therefore governs even though the Commission's order results in an allegedly confiscatory rate. See Br. in Opp., p. 8. In *United States v. Capital Transit Co.*, 338 U.S. 286, this Court brushed such a claim aside as not properly presented (338 U.S. at 291):

> It is also argued here that the orders should be set aside because they are confiscatory. But

[18] Indeed, in the very order under review the Commission disallowed certain director and executive committee payments as being improper charges under the particular facts and circumstances of Colorado (but not such rulings as to bar all exclusion

refusing to give its approval to the merger; and at all times during the rate investigation Colorado itself had accepted the condition's validity without question.

Moreover, even if the assignments had attacked the exclusion of the loss generally, so that they might conceivably be read as encompassing the condition's validity, they still would have been insufficient in this case. Cf. *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U. S. 253, 255; *National Labor Relations Board* v. *Seven-Up Co.*, 344 U.S. 344, 350. In the latter decision, this Court held that the company's general objection, that the Trial Examiner's recommendations as to the back pay "were contrary to, and unsupported by, the evidence and contrary to law," was "not adequate notice that the Company intends to press the specific issue it now raises" (344 U. S. at 350), *i. e.*, the effect of the seasonal nature of its business on the validity of the Commission's formula computing the back pay due to the employees to be reinstated. And while in *May Stores Co.* v. *National Labor Relations Board*, 326 U. S. 376, a general objection, although falling "short of desirable specificity" (see 326 U. S. at 386-387, fn. 5), was accepted by this Court as sufficient to preserve the issue there involved, this acceptance was based, in large measure, upon the peculiar circumstances of the case, particularly the fact that the issue had been a frequent subject of dispute in the Courts of Appeals. 326 U.S. at 386-387, fn. 5. In the instant case, however, the history of the condition, as we have already pointed out, is such that a general ob-

> the record fails to show that this issue was properly presented to the Commission for its determination. Therefore the question of confiscation is not ripe for judicial review.

See, also, *Todd* v. *Securities and Exchange Commission*, 137 F. 2d 475, 478 (C.A. 6), and *National Labor Relations Board* v. *G. W. Thomas Drayage & Rig. Co.*, 206 F. 2d 857, 860-861 (C.A. 9), where courts of appeals declined to consider a constitutional issue not raised before the administrative agency.[17]

3. The strength of the reasons for insisting that courts refrain from considering issues not raised before the administrative agency is shown by the

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[17] While it is not strictly relevant to the issue here presented, it may be noted in passing that the exclusion of the loss in fact reflected an appropriate "balancing of the investor and the consumer interests" by the Commission (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. at 603) and so was fully consonant with the "end-result" principle. During the pendency of the rate proceedings, there was a public offering of Colorado's common stock with full disclosure to prospective investors that the loss under the merger condition would not be "considered as a cost of service to Colorado's natural-gas consumers," but would be borne by the investors (Tr. 2685, 2694). Notwithstanding this, the common stock was promptly over-subscribed. As the Court of Appeals noted in sustaining the Commission's finding that 5¾% is a fair rate of return (R. 277):

> The fact that this offering was promptly oversubscribed is evidence of the standing of Colorado with the investing public and, if we must as urged by Colorado take into account that the eagerness to purchase this stock was induced in the belief of the future development of Colorado's resources, we must on the other hand not be unmindful that that manifested interest was in the face of a rate bearing which might well, as it did, result in a decrease of rates.

jection would plainly fail to advise the Commission of Colorado's intention to press the specific issue of the condition's validity.

Nor was the deficiency cured by the circumstance, pressed by Colorado (Br. in Opp., pp. 5-6, 11), that the condition's validity was raised in the *merger* proceeding and there considered by the Commission. In this connection it should first be recalled that, unlike many of the comparable provisions relating to judicial review of administrative action,[8] the Natural Gas Act (and the Federal Power Act, Section 313 (b), 16 U.S.C. 825*l* (b)) requires not merely that the issue be raised at some point during the administrative proceeding but prescribes a specific stage at which the objection must be made, *i.e.* in an application for rehearing before the Commission. Therefore, even if the question of the condition's legality had been raised during the administrative hearings in connection with the *rate* investigation—let alone the antecedent *merger* proceeding—Colorado's failure to preserve the issue by assigning it as error in its application for rehearing on the Commission's rate order would operate, under the express terms of Section 19(b), to foreclose the courts from considering the question.

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[8] See *e.g.*, Section 9(a) of the Securities Act of 1933, 15 U.S.C. 77i(a); Section 322 of the Trust Indenture Act, 15 U.S.C. 77vvv; Section 25(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78y(a); Section 24 of the Public Utility Holding Company Act, 15 U.S.C. 79x; Section 10(a) of the Fair Labor Standards Act, 29 U.S.C. 210(a); Section 10(e) of the National Labor Relations Act, 29 U.S.C. 160(e); Section 1006(e) of the Civil Aeronautics Act, 49 U.S.C. 646(e).

decisions following that rule even in the absence of a statutory provision like Section 19(b). For instance, the statute providing for review of Interstate Commerce Commission orders (now 28 U.S.C. 2321-2325) contains no prohibition against judicial consideration of questions not presented to the Commission, but the Court has nevertheless held that failure to apprise the Commission of an issue forecloses judicial review of that point. See *United States* v. *Tucker Truck Lines*, 344 U. S. 33, 36-37; *United States* v. *Capital Transit Co.*, 338 U. S. 286, 291; *United States* v. *Hancock Truck Lines*, 324 U. S. 774, 779-780; *United States* v. *Northern Pacific Ry.*, 288 U. S. 490, 494. The same principle was applied in *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143, 155, where the Court said: "A reviewing court usurps the agency's function when it sets aside the administrative determination upon a ground not theretofore presented and deprives the Commission of an opportunity to consider the matter, make its ruling, and state the reasons for its action." See also *United States ex rel. Vajtauer* v. *Commissioner*, 273 U. S. 103, 113.

The importance of the policy is also suggested by its close relationship to the settled principle that administrative remedies be exhausted before there may be resort to the courts.[18] Insistence on ex-

[18] Analytically, the two principles are but different facets of the same general rule. While one is applicable before the completion of the administrative proceeding and the other is controlling after completion, both preclude the courts from

But perhaps the more decisive answer to this point is that while the condition's validity was questioned in the merger proceeding, it was not challenged by Colorado. On the contrary, Colorado vigorously defended the condition which it had itself proposed to the Commission. At that time, Colorado was very anxious that the Commission adopt the condition, for approval of the merger was in substantial measure dependent thereon. Colorado's present position (adopted for the first time after the original opinion of the Court of Appeals in this case), that the condition involved "a plain and fundamental error of law" and that it was "ineffective * * * from the standpoint of substantial justice" (Br. in Opp., p. 9), is a far cry from the view expressed at the merger proceeding where Mr. William A. Dougherty, Colorado's general counsel and one of its directors, stated (R. 323):

> * * * so far as I was concerned as a director of Colorado Interstate and as its counsel * * * I would be perfectly willing to vote for as a director and to recommend to the board as its counsel that some sort of a stipulation or condition to the certificate be accepted by the company which in effect would provide this: * * * [9]

[9] Mr. Dougherty later said (R. 324):

> The treatment that I have in mind, which I say as a director I would vote for and as counsel would recommend, is that whenever these figures indicated that a net loss had occurred that that would not be charged in effect against the intervenors but the risk of that taken by the stockholders, but that there likewise should be a corre-

haustion of the administrative procedure reduces the judicial burden since in many instances the issues sought to be raised may be disposed of by the agency, rendering resort to the courts unnecessary. Cf. *Aircraft & Diesel Corp.* v. *Hirsch*, 331 U. S. 752, 772. Also, the administrative proceedings serve to define more precisely the nature of the controversy and provide a more complete context for decision. *Aircraft & Diesel Corp.* v. *Hirsch*, *supra*. Moreover, where the issue is factual, its resolution is for the agency, whose decision is binding on the courts if supported by substantial evidence; and where a purely legal question is raised, deference is to be accorded to the construction given by the expert agency charged with the statute's administration. See, *e. g.*, *Rochester Telephone Corp.* v. *United States*, 307 U. S. 125, 146; *Gray* v. *Powell*, 314 U. S. 402; *Shields* v. *Utah Idaho Central R. R.*, 305 U. S. 177; *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143.

To sanction the invalidation of the merger condition by the reviewing court—after Colorado had affirmatively proposed the condition to the Com-

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passing on issues which have not been raised before or considered by the administrative agency. This Court's recognition of the close relationship between these doctrines was manifested in the *Aragon* case, *supra*, where, referring to a statutory provision phrased in terms of exhaustion of administrative remedies (see 329 U. S. at 155, fn. 15), the Court applied the rule prohibiting judicial consideration of issues not raised before the administrative agency. For this reason, among others, the attempted distinction by the court below of the *Aragon* case (R. 301) is without any substance.

There could hardly be plainer evidence that Colorado's counsel expressed no doubt as to the legality of the condition during the merger proceeding.

In these circumstances, particularly since Colorado proposed the terms of the condition to be incorporated into the order approving the merger (*supra*, pp. 4-5), the situation here is far stronger for preclusion of the issue from judicial consideration than if there were merely involved a failure to raise the point, or even acquiescence. And it is settled that acquiescence or waiver is sufficient to bar court review, without regard to whether the statute requires that the issue be raised before the agency. See *United States* v. *Hancock Truck Lines*, 324 U.S. 774, 779-780; *United States* v. *Tucker Truck Lines*, 344 U.S. 33, 36-7; cf. *Helvering* v. *Wood*, 309 U.S. 344, 348-349.[19] See also *infra*, pp. 53-54.

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sponding credit given to the stockholders whenever the tax benefits were greater.

[19] The same principle of preclusion is reflected in the settled rule that a party who accepts the benefit of an administrative decision and puts it into effect, to his own advantage, cannot thereafter deny the validity of the conditions imposed on him by the decision. See, e.g., *Callanan Road Co.* v. *United States*, 345 U.S. 507, 513; *Fahey* v. *Mallonee*, 332 U.S. 245, 255; *United States* v. *San Francisco*, 310 U.S. 16, 29; *United Fuel Gas Co.* v. *Railroad Commission*, 278 U.S. 300, 307-308; *Booth Fisheries* v. *Industrial Commission*, 271 U.S. 208; *Buck* v. *Kuykendall*, 267 U.S. 307, 316; *St. Louis Malleable Casting Co.* v. *George C. Prendergast Construction Co.*, 260 U.S. 469; *Wall* v. *Parrot Silver & Copper Co.*, 244 U.S. 407, 411-412; *Shepard* v. *Barron*, 194 U.S. 553; *Grand Rapids and Indiana Railway Co.* v. *Osborn*, 193 U.S. 17, 29; *Daniels* v. *Tearney*, 102 U.S. 415, 421.

mission in order to obtain Commission approval of the merger and had never attacked it in the Commission's rate investigation—would be contrary to the policy considerations on which the requirements of exhaustion and of obtaining an administrative determination are based. If Colorado had joined the Commission staff in attacking the condition in the merger proceeding, it is doubtful whether the Commission would have imposed the condition upon Colorado; and it is also doubtful that it would have been willing to give its approval without such a condition. In either event, the result would have been that there would be no need for judicial consideration of the condition. On the other hand, if the Commission had undertaken to impose the condition over Colorado's objection, it would have done so on the basis of adequate justification in the record, *i.e.*, that the benefits to be derived from the merger outweighed the contingent burden being imposed upon the stockholders.

As it is, the Commission, in linking its approval of the merger to the condition, relied on the fact that the condition was proposed by Colorado which was to be subject to it. The result is that, in upsetting the condition, the court below has made a completely *de novo* examination of the issues without the benefit of an independent analysis by the experienced agency, without regard to the proper scope and method of review of administrative determinations, and on the basis of a record which was made in an

3. Section 19(b) is as fully effective in rate cases as in others; it does not become inoperative because, as the court below asserted, "the important and deciding factor in rate hearings is the end result" and "a reviewing court is more concerned with the end result than with the multiple detailed mechanics employed in reaching it" (R. 271). But the rule is the same for the "end result" of a rate order: it is not open to court review unless challenged and then only to the extent of the challenge. *Colorado Interstate Gas Company* v. *Federal Power Commission*, 324 U.S. 581, 605-606; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U.S. 635, 649; *United States* v. *Capital Transit Co.*, 338 U.S. 286, 291. Here, while Colorado objected to the "end result" reached by the Commission (R. 103), the objection was summary and general, not directed at the Commission's exclusion of the loss by virtue of the condition. As indicated *supra*, pp. 20-21, such a general objection failed in the circumstances to apprize the Commission that this specific issue was being challenged in any way, even subordinately. The "end result" standard for testing utility rates (*Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602; *Colorado Interstate Co.* v. *Federal Power Commission*, 324 U.S. 581, 603) does not nullify the requirement of specific assignments of error, or mean that a single objection to the "end result" is sufficient to enable the utility to raise any or all points that may later occur to its counsel. If that were the case, Section

other proceeding and addressed to other issues.[19] This is precisely the kind of result this Court has long been at pains to avoid in settling the rules for review of administrative orders or actions.

C. THE ADMINISTRATIVE PROCEDURE ACT DOES NOT DO AWAY WITH THE NECESSITY OF COMPLIANCE WITH SECTION 19(b)

Another error of the court below is in reading the Administrative Procedure Act as, in effect, eliminating the necessity for preserving objections before the administrative agency. The court held that the Act contained "clear and positive mandates" to the courts to consider all questions of "legality or constitutionality" inherent in a case.

1. In so holding, the court undertook to distinguish some of the cases relied on by the Commis-

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[19] The decision of the court below invalidating the condition caused both the Commission and Colorado to incorporate references from the record in the merger proceedings in their pleadings filed with the court subsequent to the decision. See, *e.g.*, Appendix A to the Commission's Petition for Rehearing (R. 289); footnote 3 and Appendix A to Brief of Petitioner [Colorado] in Response to Respondent's [Commission's] Petition for Rehearing (R. 311, 322). It is fundamentally at odds with the whole design of administrative review that facts outside the record should become part of the record in this fashion, especially where there is no reasonable excuse for the failure to adduce such facts. Such piece-meal and one-sided record-making does not afford an opportunity to introduce all the facts and facets, nor afford opportunity for cross-examination or rebuttal, and entirely by-passes the agency and does not afford it the opportunity to consider the issue, and make its findings, conclusions and rulings. All this is aside from the fact that, if Colorado were dissatisfied with the merger condition, the entire record in that proceeding was available for review in that proceeding. *Infra*, pp. 53-54.

19(b) of the Gas Act (and comparable provisions in other utility legislation) would be rendered meaningless, and the Commission and similar regulatory agencies would find themselves having to guess at, and deal with, all the points the company might subsequently raise. Quite properly, the courts have not interpreted the "end result" standard as doing away with the requirement of specific specifications of error. See, *e.g.*, *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U.S. 635, 649. The only effect of the "end result" test on the specific assignments is that their validity must be examined in the light of the impact of the alleged error on the "end result", but they must still be stated in order that they may be so examined.

B. THE COURT OF APPEALS HAD NO INHERENT POWER TO CONSIDER THE CONDITION'S VALIDITY IN THE ABSENCE OF COMPLIANCE WITH SECTION 19(b) OF THE GAS ACT

The Court of Appeals also erred when it held that, even if there had not been compliance with Section 19(b), the reviewing court nevertheless has inherent power *sua sponte* to consider and correct errors lurking in the record made before the Commission.

1. In so holding, the court confused its functions *vis a vis* the District Courts with its relationship to administrative agencies. While the Courts of Appeals have such inherent power in reviewing

sion on the ground that they antedate the Administrative Procedure Act (R. 302). But while some of the decisions cited *supra*, p. 28 were decided prior to that Act, this Court in several later decisions has recognized the continued vitality of the requirement and has reaffirmed the earlier rulings. Thus, the principle was applied in *United States* v. *Capital Transit Co.*, 338 U. S. 286, 291, and *National Labor Relations Board* v. *Seven-Up Co.*, 344 U. S. 344, 350, both cases decided several years after the Act's passage.

Of particular relevance on this point is *United States* v. *Tucker Truck Lines*, 344 U. S. 33. The *Tucker* case was decided a number of years after the enactment of the Administrative Procedure Act, and, significantly, the issue sought to be raised revolved about that Act itself, *i.e.*, the failure of the Interstate Commerce Commission to comply in its administrative proceeding with the hearing examiner requirement of Section 11, previously held to be "jurisdictional" (*Riss & Co.* v. *United States*, 341 U. S. 907; *Wong Yang Sung* v. *McGrath*, 339 U. S. 33). In holding that Tucker's failure to complain of the lack of compliance with Section 11 before the Commission precluded judicial consideration of the alleged error, the Court plainly ruled that the Act had not abrogated the well-established principles which we have discussed above (344 U. S. at 36-37):

> We have recognized in more than a few decisions, and Congress has recognized in more than a few statutes, that orderly procedure and

judgment of District Courts,[1] their jurisdiction over administrative action is narrower, and is defined by the statutory provisions authorizing the review. *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134, 141; *Switchmen's Union* v. *National Mediation Board*, 320 U. S. 297, 300-301; *National Labor Relations Board* v. *Cheney Lumber Co.*, 327 U. S. 385, 388-389; *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143, 155; *Federal Power Commission* v. *Pacific Power & Light Co.*, 307 U. S. 156, 159; *Universal Camera Corp.* v. *National Labor Relations Board*, 340 U. S. 474, 487 *ff.* As stated by Mr. Justice Frankfurter, dissenting in *Stark* v. *Wickard*, 321 U. S. 288, 312:

> Except in those rare instances, as in a claim of citizenship in deportation proceedings * * *, whether judicial review is available at all, and, if so, who may invoke it, under what circumstances, in what manner, and to what end, are questions that depend for their answer upon the particular enactment under which judicial review is claimed.

Section 19(b) of the Natural Gas Act, which vests in the Courts of Appeals whatever authority

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[1] Although the power exists on review of district court decisions, the usual practice is not to consider such new issues. "This practice is founded upon considerations of fairness to the court and to the parties and of the public interest in bringing litigation to an end after fair opportunity has been afforded to present all issues of law and fact." *United States* v. *Atkinson*, 297 U. S. 157, 159.

> good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts.

See also *supra*, pp. 27-32. The fact that the statutes applying to review of Interstate Commerce Commission orders do not contain an express provision requiring such a result (see *supra*, pp. 36-37) would seem to make the result *a fortiori* where, as here, the statute does embody a specific requirement that the issue be first raised before the agency.

Similarly, the Courts of Appeals have assumed this Court's earlier rulings to be unaffected by the Administrative Procedure Act, and have continued to insist that issues sought to be raised before them must first have been brought to the attention of the administrative agency. See, *e.g.*, *Halsted* v. *Securities Exchange Commission*, 182 F. 2d 660, 669 (C.A. D.C.); *West Texas Utilities Co.* v. *National Labor Relations Board*, 184 F. 2d 233, 239-240 (C.A. D.C.); *National Labor Relations Board* v. *Townsend*, 185 F. 2d 378, 380-381 (C.A. 9), certiorari denied, 341 U. S. 909; *National Labor Relations Board* v. *Noroian*, 193 F. 2d 172, 173 (C.A. 9); *National Labor Relations Board* v. *Auburn Curtain Co.*, 193 F. 2d 826, 827 (C.A. 1); *National Labor Relations Board* v. *Pugh & Barr, Inc.*, 194 F. 2d 217, 220-221 (C.A. 4); *United States ex rel. Beck* v. *Neelly*, 202 F. 2d 221, 224 (C.A. 7); *National Labor Relations Board* v. *Pinkerton's National De-*

they have to review orders of the Commission under that Act, on its face prohibits *sua sponte* consideration of errors found by the court to be lurking in the record. It provides that "No objection * * * shall be considered *by the court* * * *" (emphasis added), and is not in terms limited to a prohibition directed at the parties. Thus, the normal reading of Section 19(b), as it is phrased, would be that it is not addressed solely to preventing the complaining party from raising new questions, but also precludes *sua sponte* consideration of such an alleged error by the court as well. Cf. *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U. S. 635, 649. The reading of Section 19(b) suggested by the court below would go a long way toward defeating the purposes of the requirement. See *infra*, pp. 31-40.

Moreover, it has been established by the decisions of this Court that provisions such as Section 19(b) are to be applied in accordance with their plain language and that there is no such distinction between court and parties as that adopted by the court below. In *National Labor Relations Board* v. *Cheney Lumber Co.*, 327 U. S. 385, where a Court of Appeals had struck out a paragraph of a Labor Board order not objected to by the company in the administrative proceeding, this Court reversed, pointing out that the provision in the National Labor Relations Act, comparable to Section 19(b) (see *supra*, p. 21 fn. 8), constituted "[a] limitation which Congress has placed upon the power of courts to review

tective Agency, 202 F. 2d 230, 233 (C.A. 9); *Democrat Printing Co. v. Federal Communications Commission*, 202 F. 2d 298, 305 (C.A. D.C.); *National Labor Relations Board v. Pappas & Co.*, 203 F. 2d 569, 571-572 (C.A. 9); *National Labor Relations Board v. G. W. Thomas Drayage & Rig. Co.*, 206 F. 2d 857 (C.A. 9). For example, in *Democrat Printing Co. v. Federal Communications Commission*, *supra*, where a radio station sought for the first time on review to invoke Section 5(c) of the Administrative Procedure Act, urging that the Section was mandatory and waiver thereof impossible, the Court of Appeals for the District of Columbia Circuit ruled (202 F. 2d at 305):

> * * * We think this position untenable. The legislative history clearly indicates the possibility of specific waiver:
>
> > "No agency action taken or refused would be lawful except as done in full compliance with all applicable provisions of the bill and subject to the judicial review provided. No agreed waiver of its provisions would suffice unless entirely voluntary and without any manner or form of coercion."[29]
>
> And waiver by non-action would reasonably follow where as here, timely objection would have given the agency an opportunity to correct errors at the threshold of the proceedings

[29] The court refers to H. Rep. No. 1980, 79th Cong., 2d Sess., p. 47; see also S. Doc. 248, 79th Cong., 2d Sess. (Legislative History of the Administrative Procedure Act), p. 281.

orders of the Labor Board" (327 U. S. at 388). By this provision "Congress has said in effect that in a proceeding for enforcement of the Board's order the court is to render judgment on consent as to all issues that were contestable before the Board but were in fact not contested * * * [the provision] 'gives emphasis to the salutary policy * * * of affording the Board opportunity to consider on the merits questions to be urged upon review of its order'" (*id.* at 389). See, also, *Marshall Field & Co.* v. *National Labor Relations Board*, 318 U. S. 253, 255-256; *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U. S. 635, 649, and 650-651 (concurring opinion of Stone, C. J.); *United States* v. *Hancock Truck Lines*, 324 U. S. 774, 779-780; *May Stores Co.* v. *National Labor Relations Board*, 326 U. S. 376, 386, fn. 5; *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143, 155; *United States* v. *Capital Transit Co.*, 338 U. S. 286, 291; *National Labor Relations Board* v. *Bradford Dyeing Ass'n*, 310 U.S. 318, 341; *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, 617; *United States* v. *Tucker Truck Lines*, 344 U. S. 33, 36-37; *National Labor Relations Board* v. *Seven-Up Co.*, 344 U. S. 344, 350; *United States ex rel Vajtauer* v. *Commissioner*, 273 U. S. 103, 113; *United States* v. *Northern Pacific R. Co.*, 288 U. S. 490, 494. In none of these cases has the Court made any distinction between the preclusion of a party from raising an issue and

which might otherwise require the subsequent invalidation of the entire proceeding.

It is also noteworthy that the Court has given no intimation that the doctrine of exhaustion of administrative remedies has been affected by the enactment of the Administrative Procedure Act. See, *e.g.*, *Allen* v. *Grand Central Aircraft Co.*, 347 U. S. 535, 540-541; *Franklin* v. *Jonco Aircraft Corp.*, 346 U.S. 868. In view of the close relationship between the exhaustion doctrine and the principle here involved (see *supra*, pp. 37-38 and fn. 18), the continued vitality of the exhaustion rule serves to buttress further our position that the companion rule precluding courts from considering objections not raised before the administrative agency is likewise unaffected by the Administrative Procedure Act.

2. Moreover the language and the legislative history of the Administrative Procedure Act indicate that that Act did not abrogate the established principle.

(a). The court below predicated its opposite conclusion solely on the bare wording of Section 10(e) that "So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions * * *. It shall * * * hold unlawful and set aside agency action, findings, and conclusions found to be * * * not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; * * *" (R. 301). Read in

the power of the reviewing court to consider it *sua sponte*.[12]

The circumstances in which the Court has insisted in several of its cases upon compliance with these statutory requirements strongly attests to their importance as conditions precedent, binding on court as well as parties, to consideration of the substantive issues. In *May Stores Co.* v. *National Labor Relations Board*, 326 U. S. 376, *supra*, no claim was made by the Board that the company had failed to raise the issue before the administrative agency, yet the Court on its own motion appraised "the record to determine the power of the Circuit Court" to consider the matter, 326 U. S. at 386, fn. 5. In *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 324 U. S. 635, *supra*, the company's failure to raise the substantive issue

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[12] *Hormel* v. *Helvering*, 312 U. S. 552, cited by Colorado (Br. in Opp., p. 14), is inapplicable here. The statutory review provision involved in that case contained the phrase, not present here, "as justice may require," a phrase which this Court read as vesting a review authority in the courts somewhat broader than that granted by the more usual statutory review provision. Moreover, and of perhaps greater importance, the error which the Court held could be considered, although not raised before the Board of Tax Appeals, was revealed by circumstances which came into being subsequent to the decision of that Board. See 312 U. S. at 559; cf. *National Labor Relations Board* v. *Jones & Laughlin Co.*, 331 U. S. 416, 427-428. Here, on the other hand, Colorado was aware of the issue at least since the time it was raised by the Commission's staff in the merger proceeding and yet Colorado itself never raised it at any time prior to the decision below. The holding in the instant case that the condition is invalid hardly constitutes such an exceptional circumstance as would justify the invocation of the *Hormel* exception.

properly was mentioned in the Commission's brief only in passing, by way of footnote. See Brief for Respondents in No. 296, Oct. Term, 1944, p. 31, n. 20. In *National Labor Relations Board* v. *Cheney Lumber Co.*, 327 U. S. 385, *supra*, the Board claimed in its petition for certiorari that the substantive issue had not been raised during the administrative proceeding (see Petition for Writ of Certiorari in No. 319, Oct. Term, 1945, pp. 22-23); however, in its brief on the merits the Board expressed doubt, after further study of the record, as to the soundness of its original position and "[w]hile we still believe that the court below erred in its action * * *, we have decided, under the circumstances, not to press this matter in this case." Brief for National Labor Relations Board in No. 319, Oct. Term, 1945, pp. 13-14. Moreover, in *Cheney*, it was argued that since it was a proceeding to enforce the Board's order, and not a straight review proceeding, the statutory prohibition was inapplicable and the Court should frame its decree according to equitable principles. See 327 U. S. at 389-391 (Stone, C. J., concurring). *In National Labor Relations Board* v. *Seven-Up Co.*, 344 U. S. 344, *supra*, likewise an enforcement case, the failure of the company to raise the substantive issue in the administrative proceeding was not questioned by the Board in its brief. See Brief for National Labor Relations Board in No. 217, Oct. Term, 1952. Notwithstanding these circumstances, this Court held in each of these cases that failure to preserve the substantive question by timely objection before

tain Co., 193 F. 2d 825, 827 (C.A. 1); *Johnson* v. *Shaughnessy*, 336 U. S. 806, 819, fn. 5 (dissenting opinion of Reed J.). These provisions, singly or together, indicate that the Administrative Procedure Act was not intended to do away with the rule precluding judicial review of issues not timely raised before the administrative agency.[22]

(b). Far from supporting the construction below, the legislative history of the Act shows that it was not designed to upset requirements such as that embodied in Section 19(b) of the Gas Act. This is apparent from the very excerpts from the legislative history quoted by Colorado (Br. in Opp., p. 14).[23] In addition, Congress's lack of intention to abrogate the principle reflected in Section 19(b) is manifested elsewhere in the legislative history. Thus, the Senate Committee, in changing the lan-

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[22] Quoting from *Pittsburgh Steamship Co.* v. *National Labor Relations Board*, 180 F. 2d 731, 736, 737 (C.A. 6), affirmed, 340 U.S. 498, Colorado relies on "the whole record" provision contained in Section 10(e) as supporting the holding below (Br. in Opp., p. 13). The quoted language relates primarily to the criteria used in reviewing administrative findings of fact, *i.e.*, whether on the whole record there is substantial evidence supporting the agency's finding. Neither the provision nor the decisions concerning it (*e.g.*, *Universal Camera Corp.* v. *National Labor Relations Board*, 340 U. S. 474) bear in any way upon the issue here involved.

[23] As there stated, "The Senate Judiciary Committee recognized that: 'The rule of review stated is that which is judicially recognized' (Sen. Com. Rep., Sen. Doc. No. 248, p. 36)" and "In the report of the House Judiciary Committee it was stated under Section 10: 'This section requires adequate, fair, effective, complete and just determination of the rights of any person in *properly invoked* proceedings.' (*Id.*, p. 275)" (emphasis added).

the agency constituted a bar to judicial consideration of the issue.[13]

2. There is likewise no justification for the Court of Appeals' refusal to accept Section 19(b) as controlling on the ground that the question here is one of law and the Section applies only to issues of fact (R. 301).

(a). In the first place, the terms of Section 19(b) (*infra*, p. 58) do not differentiate between issues of fact, issues of law, or mixed questions of fact and law. All are covered under the general rubric of "objection[s] to the order of the Commission". And the important aims of the provision require that it apply to all issues alike. The agency charged with administering the Act should have the opportunity to "consider the matter, make its ruling, and state the reasons for its action" (*Unemployment Compensation Commission* v. *Aragon*, 329 U.S. 143, 155); "orderly procedure and good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts" (*United States* v.

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[13] An interesting sidelight to the *Cheney* case is the fact that, subsequent to this Court's reversal, the Court of Appeals for the Ninth Circuit reconsidered its judgment in at least two additional Labor Board cases and, in the light of *Cheney*, modified its decree to enforce provisions of the Board's order not questioned before the Board. See *National Labor Relations Board* v. *Van De Kamp's Holland-Dutch Bakers, Inc.*, 154 F. 2d 828, modifying 152 F. 2d 815; *National Labor Relations Board* v. *Kromo Motors*, 154 F. 2d 1007, modifying 152 F. 2d 816.

guage of Section 10(c) to its present form, explained the purpose of the change as follows (S. Doc. No. 248, 79th Cong., 2d Sess., p. 289, fn. 21):

> The change is made to clarify the provision by making specifically the language of the bill the explanation given in the Senate Committee report (p. 27). It should be noted that section 8(a) permits agencies to provide by rule for appeals to them from initial decisions of examiners. That provision, as well as this provision of section 10(c), would authorize an agency to adopt rules requiring a party to take a timely appeal to the agency before resorting to the courts. *A party cannot willfully fail to exhaust his administrative remedies and then, after the agency action has become operative, either secure a suspension of the agency action by a belated appeal to the agency, or resort to court without having given the agency an opportunity to determine the questions raised. If he so fails he is precluded from judicial review by the application to the time-honored doctrine of exhaustion of administrative remedies.* * * * [Emphasis added.]

Similarly, Senator McCarran, the principal Senate proponent of the bill, stated in response to a question (S. Doc. 248, 79th Cong., 2d Sess., p. 311):

> * * * in answer to the first part of the Senator's question, namely, where a review is precluded by law—we do not interfere with the

Tucker Truck Lines, 344 U.S. 33, 37). See also *infra*, pp. 36-42.

Accordingly, the Court has not made the distinction put forward by the court below. In the *Marshall Field* case, 318 U. S. 253, the question which this Court held could not be considered because not raised before the Labor Board related to the Board's power to grant a back pay order barring the deduction of unemployment compensation from the award. In *Panhandle Eastern Pipe Line*, 324 U.S. 635, the problem was whether the exemption of Section 1(b) of the Natural Gas Act deprived the Commission of authority to include production and gathering facilities at original cost in the rate base for jurisdictional sales. In the *Tucker Truck Lines* case, 344 U.S. 33, the issue concerned the validity of a hearing, subject to the Administrative Procedure Act, held before an examiner not appointed pursuant to Section 11 of that Act (5 U.S.C. 1010). The issue in each of these cases was clearly "legal" in nature, yet the failure to raise it before the administrative agency was held to preclude judicial consideration. Cf. the rule on exhaustion of administrative remedies, as applied in *Macauley* v. *Waterman Steamship Corp.*, 327 U.S. 540, 544; *Aircraft & Diesel Corp.* v. *Hirsch*, 331 U.S. 752; *Federal Power Commission* v. *Arkansas Power & Light Co.*, 330 U.S. 802; see infra, pp. 37-38.[19]

[19] Colorado's contention that the rule is inapplicable since the [illegible] by granting rehearing has afforded" the Commission an "opportunity to reconsider its side of the case on the

(b). Secondly, the particular issue involved here cannot be viewed in its proper context as purely "legal." The propriety of the exclusion of the loss was to be tested not solely against the infirmities, if any, in the exclusion itself, but rather by the test of whether the consequence of the exclusion was such as to make "the total effect of the rate order * * * unjust and unreasonable." *See Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602. This, in turn, depends on whether the rates fixed by the Commission "enable the company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risks assumed * * *" *(id.* at 605). The evaluation of the financial data necessary to ascertain the reasonableness *vel non* of the "end result" can hardly be said to present a pure question of law which need not be passed upon in the first instance by the agency experienced in the marshalling and evaluation of such data. *Cf. National Labor Relations Board* v. *Hearst Publications, Inc.*, 322 U.S. at 130; *Unemployment Compensation Commission* v. *Aragon*, 329 U.S. at 153-154; *National Labor Relations Board* v. *Seven-Up Co.*, 344 U.S. at 349-350.

In addition, there is more than a conclusion of law involved in deciding even the narrower issue of whether the exclusion of the gasoline loss, pur-

question" (R. 313) does not limit analysis. Similar "opportunities" in the reviewing court would have been afforded the administrative agency in each of the cases referred to in the text, yet in each case this Court held that the courts were limited from considering the ultimate end.

context with the other provisions of the statute, this language does not have the scope attributed to it below.

In the first place, subsection (e), along with the other subsections of Section 10, is subject to an introductory clause (*infra*, p. 58) which expressly makes Section 10 inapplicable where "statutes preclude judicial review." This language precludes judicial review not only where the relevant statute forecloses review entirely, as Colorado suggests (Br. in Opp., p. 14), but also where, as here, the relevant review provision precludes review of specific issues not raised before the administrative agency. Cf. *Heikkila* v. *Barber*, 345 U.S. 229.[21] Moreover, subsection (e), which is captioned "Reviewable Acts" in contrast to subsection (e)'s caption of "Scope of Review," provides at the outset "Every agency action made reviewable by statute * * * shall be subject to judicial review." And the very language relied on by the court below is to the effect that the court's are to "decide all relevant questions of law," but only "where presented," a phrase which might very well have been intended to limit the scope of review to situations where the issues are properly presented by virtue of having been preserved before the administrative agency. See also Sections 7(c), 8(b)(2) and 10(b) of the Act; cf. *National Labor Relations Board* v. *Auburn Car-*

[21] A detailed argument in support of this proposition is set forth in the Government's briefs in *Blackmar* v. *Guerre*, Oct. Term 1951, No. 361, at pp. 26 *ff.* and *Martinez* v. *Nevills*, Oct. Term 1952, No. 218, at pp. 26 *ff.*

> statute, anywhere in this bill. Substantive law, law enacted by statute by the Congress of the United States, granting a review or denying a review is not interfered with by this bill. We were not setting ourselves up to abrogate acts of Congress.[24]

In the same vein are the statements of Congressman Walter, the principal proponent of the bill in the House. In his analysis of the bill in the House, he stated that Section 10(b) "does not disturb special proceedings which Congress has provided" and further that the provision of Section 10(c) "are technical but involve no departure from the usual and well-understood rules of procedure in this field" (*id.*, at 369). See also *id.*, at p. 374 (statement of Representative Gwynne); pp. 229-230 (statement of the Attorney General); also *supra*, pp. 43-44.

D. THE COURT OF APPEALS ERRONEOUSLY EXERCISED AN ADMINISTRATIVE FUNCTION IN INVALIDATING THE CONDITION ON WHICH THE COMMISSION HAD PREDICATED ITS APPROVAL OF THE MERGER

Finally, the ruling below is erroneous for the further reason that, since its effect is to leave the merger outstanding without the condition, the Court of Appeals thereby infringed upon the administrative functions of the Commission, in violation of the long-settled principle most recently

[24] See also *id.*, at p. 307.

iterated in *Federal Power Commission* v. *Idaho ower Co.*, 344 U. S. 17, 20-21, that it is for the gency, not the reviewing court, to determine hether the agency's approval should stand if a ndition of the approval is stricken as unlawful. In the *Idaho Power* case, the Commission had ued a license for the construction and operation a hydroelectric project on the condition, among hers, that the licensee permit the transmission er its lines of power generated at government-ned power plants. The Court of Appeals, lding that the Commission had no authority impose the condition, struck out the condi-n and in effect directed the Commission to grant e license without the condition. This Court re-rsed, pointing out that the decision by the Court Appeals that the license should issue without the ndition constituted an usurpation of the admin-trative function (344 U. S. at 20). "The nature the determination," this Court stated (*id.* at 21), s emphasized by § 10(a) which specifies that the

[1] Accord: *Federal Trade Commission* v. *Morton Salt Co.*, U. S. 37, 50; *Siegel Co.* v. *Federal Trade Commission*, 327 S. 606, 612-614; *Addison* v. *Holly Hill Co.*, 322 U. S. 607, 617-619; *Federal Communications Commission* v. *Pottsville Broadcasting Co.*, 309 U. S. 134, 145; *Cudahy Co. Corporation* v. *Alcoholic Terminal Co.*, 308 U. S. 422, 432-433; *Ford Motor Co.* v. *National Labor Relations Board*, 305 U. S. 364, 373-374; *St. Louis, Brownsville & Mexico Ry. Co.* v. *Brownsville Navigation District*, 291 U. S. 295, 301; *Federal Trade Commission* v. *Royal Milling Co.*, 288 U. S. 212, 215; *Southern Ry. Co.* v. *Tift*, 206 U. S. 428, 435-436; *Texas & Pac. Ry. Co.* v. *Abilene Cotton Oil Co.*, 204 U. S. 426, 444-445; cf. *Pan East Corporation* v. *United States*, 312 U. S. 570, 574-575.

project adopted 'shall be such as in the judgment of the Commission will be best adapted to a comprehensive plan * * * for the improvement and utilization of water power development, and for other beneficial public uses.' Whether that objective may be achieved if the contested conditions are stricken from the order is an administrative, not a judicial decision."

Similarly, in the present case the determination whether to authorize the merger and on what conditions is clearly an administrative function of the Power Commission. Section 7(e) of the Natural Gas Act, *infra*, pp. 56-57, explicitly provides:

> Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or *acquisition* covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or *acquisition*, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. *The Commission shall have the power*

to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require (emphasis added).

It was therefore for the Commission, not the Court of Appeals, to decide whether the merger should be allowed to stand if the challenged condition were excised.

In addition, the circumstances surrounding the imposition of the condition are, as we have already indicated, very significant. The condition was imposed by the Commission in the prior merger proceeding. During that proceeding the Commission was troubled by the possibility that the merger, if approved, might result in Colorado's gas customers having to bear losses suffered by Colorado in conducting the gasoline operations. Since this possibility raised a substantial obstacle to approval of the merger, Colorado, to obviate the objection, suggested to the Commission that its approval be conditioned on the exclusion of these losses, if any should be incurred, from the costs of service (R. 289-290). Such a condition, Colorado represented, "would adequately protect ultimate consumers" (R. 289). The Commission accordingly approved the merger on this condition (among others) with the condition obviously being an important element relied on by the Commission in concluding that the merger, so conditioned, would be in the public interest. In these circum-

stances, it was plain error for the court below to strike down the condition while permitting the merger itself to remain in effect, for here, as in *Idaho Power*, the determination whether the objectives of Section 7 are achieved with the condition stricken is an administrative, not a judicial, matter.

A superficial argument may perhaps be made that the *Idaho Power* line of cases supports the court's ruling rather than the Commission's position. In these cases, this Court has held that, once the error of law has been laid bare, the appropriate procedure is to remand the case to the administrative agency for consideration in the light thereof. This procedure, it may be said, has been followed here, for the Court of Appeals remanded the case to the Commission for consideration in the light of the invalidity of the condition. But such an argument ignores the critical fact that the condition was imposed in another proceeding, not in the rate investigation, and that the remand here was merely to enable the Commission to make the appropriate adjustments in its rate order, not to determine whether to approve the merger without the condition.[26] Since this proceeding is not a re-

[26] Indeed, the merger order had long since become final and the merger there approved has been accomplished. To reconsider the propriety of the merger without the condition would, should the Commission determine that the merger would not be in the public interest without the condition, raise both legal and practical problems relating to the dissolution of the merger.

view of the merger order and the court below was without authority to direct reconsideration of that order, the court below should properly have accepted the merger condition without question, as had Colorado as well as the Commission, and reviewed the Commission's rate order on that basis.[27]

Nor is there merit to Colorado's claim (Br. in Opp., p. 16) that it could not have sought direct review of the merger condition because it first became ripe for judicial consideration in the rate investigation. As shown *supra*, pp. 22-23, 51, Colorado was in no position to seek review of the condition; having suggested the condition to the Commission and thereby having more than acquiesced, Colorado was in effect estopped from challenging the condition. *United States* v. *Hancock Truck Lines*, 324 U. S. 774, 779, 780; *Helvering* v. *Wood*, 309 U. S. 344, 348, 349.[28] And if Colorado were not so estopped, the condition would have been subject to

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[27] It is generally agreed that where there is an exclusive statutory provision for direct review, representing "a distinctive formulation of the conditions under which resort to the courts may be made" (*Federal Power Commission* v. *Pacific Power & Light Co.*, 307 U. S. 156, 159), collateral attack upon the agency's action is not permitted. See, *e.g.*, *Louisville Gas & Electric Co.* v. *Federal Power Commission*, 129 F. 2d 126 (C.A. 6); *Woods* v. *Kane*, 175 F. 2d 886 (C.A. 9); *Miles Laboratories* v. *Federal Trade Commission*, 140 F. 2d 683, 684 (C.A. D.C.), certiorari denied 322 U. S. 752.

[28] It is an established principle of law that a party who has accepted a grant, privilege, or license, including conditions imposed by the administrative agency, cannot attack the conditions after having put into effect and taken the advantages of the grant, privilege, or license. See fn. 10, *supra*, p. 23.

direct review in the merger proceeding for the same reasons that the condition involved in the *Idaho Power* case was ripe for immediate direct review; consequently, Colorado's failure to seek such review resulted in the Commission's action being conclusive and binding in this subsequent rate proceeding.

In *Idaho Power*, as here, the condition was not in a sense immediately operative since the transmission lines which were to carry the government power had not yet been constructed; here, the loss from gasoline operations was not to be excluded until its existence was determined in the rate investigation. Yet the fact that the provisions were tied in with, and imposed as conditions of, the approval of the Commission—the benefits of which were to accrue to the company immediately—made it imperative in *Idaho Power*, as here, that any question as to the validity of the condition (and of the approval based thereon) be raised and passed upon in a direct review. Any other result would place those to whom the Commission has given a conditional approval in the position, which Colorado is seeking to establish for itself here, of being able to reap the full benefits of the approval while reserving the right to attack the condition at some future time when it might no longer be feasible, as a practical matter, for the Commission to withhold its unconditional approval.

CONCLUSION

For the foregoing reasons, the judgment of the court below should be reversed to the extent that it invalidates the condition pursuant to which the Commission excluded from cost of service Colorado's losses from the gasoline operations.

Respectfully submitted.

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OCTOBER, 1954.

APPENDIX

1. The Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717 *et seq.*, provides in pertinent part:

* * * * * * *

SEC. 7.

(c) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations * * *.

* * * * * * *

(e) Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the

Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require.

* * * * * * *

SEC. 19. (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State municipality or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. * * * No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein

the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

2. The Administrative Procedure Act, 60 Stat. 237, 5 U.S.C. 1001 *et seq.*, provides in pertinent part:

SEC. 10. * * * * * *

(b) *Form and Venue of Action.*—The form of proceeding for judicial review shall be any special statutory review proceeding relevant to the subject matter in any court specified by statute or, in the absence of inadequacy thereof, any applicable form of legal action (including actions for declaratory judgments or writs of prohibitory or mandatory injunction or habeas corpus) in any court of competent jurisdiction. Agency action shall be subject to judicial review in civil or criminal pro-

Sec. 10. Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion --

ceedings for judicial enforcement except to the extent that prior, adequate, and exclusive opportunity for such review is provided by law.

(c) *Reviewable Acts.*—Every agency action made reviewable by statute and every final agency action for which there is no other adequate remedy in any court shall be subject to judicial review. Any preliminary, procedural, or intermediate agency action or ruling not directly reviewable shall be subject to review upon the review of the final agency action. Except as otherwise expressly required by statute, agency action otherwise final shall be final for the purposes of this subsection whether or not there has been presented or determined any application for a declaratory order, for any form of reconsideration, or (unless the agency otherwise requires by rule and provides that the action meanwhile shall be inoperative) for an appeal to superior agency authority.

* * * * *

(e) *Scope of Review.*—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary,

capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

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No. 45

In the Supreme Court of the United States

OCTOBER TERM, 1954

FEDERAL POWER COMMISSION, PETITIONER

v.

COLORADO INTERSTATE GAS COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

REPLY BRIEF FOR THE FEDERAL POWER COMMISSION

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INDEX

CITATIONS

Cases:	Page
Marshall Field & Company v. *National Labor Relations Board*, 318 U. S. 253	9
May Stores Co. v. *National Labor Relations Board*, 326 U. S. 376	9
National Labor Relations Board v. *Seven-Up Bottling Co.*, 344 U. S. 344	9
Transcontinental Gas Pipe Line Corporation, In re, F. P. C. Docket G-1842	3, 6
Statute:	
Natural Gas Act, 52 Stat. 821, as amended, 15 U. S. C. 717, *et seq.*:	
Section 19 (b)	1, 4, 8

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

REPLY BRIEF FOR THE FEDERAL POWER COMMISSION

We believe that our main brief disposes of the various contentions advanced by Colorado. However, since the Company strenuously presses arguments predicated on the specification, in its application for rehearing, in regard to the Commission's calculation of the income tax component of the cost of service, further elaboration on this point, beyond the summary comment in our main brief (p. 17, fn. 6), may be helpful to the Court.

The argument in Colorado's brief based on this specification is not completely clear. While the primary contention appears to be that this specification was sufficient under Section 19 (b) of the Natural Gas Act to preserve for judicial review the

question of the validity of the merger condition (Br. pp. 15–19), there are also indications in the brief (see e. g., pp. 12, 15) that Colorado's point is that, although the assigned error as to the income tax component was not the basis of the Court of Appeals' reversal, the error thus assertedly committed by the Commission constitutes an alternative and separate justification for that judgment. Each of these arguments is without merit.

1. Taking the second contention first, it is clear that the alleged error as to the income tax component cannot constitute an alternative ground for the reversal below. The exclusion of the $456,665 item of income tax from the cost of service stemmed from the Commission's finding of a $420,000 loss from gasoline operations. Since this loss was, under the merger condition, to be excluded from cost of service, the result was to reduce Colorado's income tax liability under the Commission's computation by $456,665. The income tax item was dependent upon the exclusion of the gasoline loss, which, in turn, depended upon the validity of the merger condition. The consequence is that the total exclusion ultimately dependent upon the validity of the merger condition embraced not only the $420,000 gasoline loss but also the related income tax, or a total (including a State income tax component of $13,700) of $892,000. See the Commission's main brief, p. 6, fn. 3. Thus, even if the Company were correct in its view as to the income tax (as

distinguished from the gasoline loss), the correctness of that contention could not support a judgment based on consideration of the entire $892,000. Moreover, the Court of Appeals expressly recognized that its holding that the merger condition was invalid and its concomitant reversal of the exclusion of the gasoline loss will "require further consideration of the item of federal income taxes as an element of the cost of service" (R. 277). These two considerations remove any possibility that the alleged error in computing the income tax component at $456,665, even if committed by the Commission,[1] could support the reversal below on the invalidity of the merger condition.

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[1] We do not, of course, concede that the Commission's calculation of the income tax component was erroneous. On the contrary, we believe the computation to be entirely correct, and consistent with the Commission's established practice of allowing as income tax the actual tax liability to be incurred. See, e. g., *In re Transcontinental Gas Pipe Line Corporation*, F. P. C. Docket G–1842, at R. 112, and p. 17 of Colorado's Br. Colorado's argument on this score appears to be that since the Commission for regulatory purposes eliminated the gasoline loss from the cost of service, the Commission should have computed the income tax liability as if the gasoline loss had not been incurred. The Commission's refusal to adopt Colorado's approach, Colorado urges, has the effect of further reducing the return allowed. But the fact is that, under Colorado's theory, its income tax liability would be artificially increased to a figure $456,665 in excess of the actual tax liability. Since this sum would be retained by Colorado, and not actually disbursed as taxes, the result would be, as the Commission pointed out (R. 127–128), that the actual return to Colorado would be increased by the $456,665 less the resulting additional income tax, and thereby offset in substantial part the gasoline loss. On the other

2. Nor is Colorado's claim any more substantial if it be that its objection in the application for rehearing to the income tax component satisfied the requirements of Section 19 (b) of the Gas Act, so as to preserve for judicial scrutiny the validity *vel non* of the merger condition.

(a) In dealing with this matter, it is important to stress Colorado's explicit admission that its specification of errors *in regard to the gasoline loss itself* "assumed" "the *propriety* of the deduction" if the loss were properly determined (Br. p. 16, fn. 10, emphasis added), and went only to "contentions in regard to the method, the failure to use the appropriate factors under the adopted method, the lack of substantial evidence to sustain the conclusion that there was a loss, and to the contention that the method adopted violated the certificate condition (R. 98–103, 106–114)" (Br. p. 16, see also pp. 2, 12). As already shown in our main brief (pp. 14–25), those assignments fall far short of satisfying the requirements of Section 19 (b) of the Gas Act, particularly when they are read against the background and history of the merger condition.

(b) Since the specifications dealing with the gasoline loss—which was directly related to the condition—did not raise the issue of the condi-

---

hand, under the Commission's approach Colorado would receive the full return to which it was entitled, less, of course, the gasoline loss in accordance with the terms of the merger condition, together with the actual taxes based thereon.

tion's validity, it is extremely unlikely that the issue would be raised by the specification dealing with the income tax component—which, while stemming from the gasoline loss, bore only indirectly upon the merger condition. And the plain fact is that the condition's validity was *not* raised by the income tax specification. On the contrary, that specification, like those dealing with the gasoline loss, appears to have accepted the condition's validity as a basic premise.

Specification No. 40, the sole specification on the income tax component, alleged merely (R. 103):

> 40. The Commission erred in not allowing to Colorado Federal Income Taxes and State Income Taxes, associated with the 5¾ per cent rate of return found by the Commission to be reasonable and, in fact the Commission has reduced the allowed rate of return from 5¾ per cent to 5.01 per cent.

Clearly, the wording of this specification fell far short of apprising the Commission that Colorado was by indirection attacking the condition, which Colorado had affirmatively pressed upon the Commission in the merger proceeding and which it had not questioned directly in the specifications dealing with the gasoline loss (see the Commission's main brief, pp. 14–25).

Nor would the discussion in the application for rehearing relative to this specification so advise the Commission. See R. 112–114. As the quotation from the Commission's opinion in *In re*

> in the cost of service of the $421,537. To accede to Colorado's contention, however, is to nullify the removal of the $421,537 from the costs which the customers of Colorado should bear. [Emphasis added.]

(c) Apparently recognizing that its income tax specification did not in and of itself attack the merger condition, Colorado argues that the Commission was apprised that the validity of the merger condition was in issue by the allegations that the Commission's action on income taxes resulted in a reduction in the Company's return and that the exclusion of the gasoline loss also had a similar result (see Colorado's Br., pp. 16–21). But, as already indicated, Colorado had alleged specific error in regard to the Commission's calculation of income taxes—an alleged error not only without bearing on the merger condition but explicitly assuming its validity. Such an allegation—even more, since more remote, than the specification on the calculation of the gasoline loss—failed to inform the Commission that the merger condition was under attack. See our main brief, pp. 18–20. Consequently, even assuming, as Colorado contends (Br. pp. 17–18), that the gasoline loss and the income taxes were fused by the Commission, the Company's assigning as error of the Commission's method of calculating income taxes falls far short of preserving for judicial review, under Section 19[a] (b), the

merger condition's validity. For Colorado's complaints as to both components of the "fusion"—gasoline loss and income tax—assumed that the condition was valid and proceeded from that point.

Moreover, to construe the income tax specification as putting the Company's return in general issue would not help Colorado here. Since there are many elements which go to make up the return, such a general assignment would not advise the Commission which of the numerous components of the return were being questioned. Certainly, it would not apprise the Commission that, having espoused the condition in the merger proceeding, Colorado had reversed its position and was now attacking the condition. For that reason, as we have pointed out in our main brief, pp. 20–21, the support which Colorado seeks from *May Stores Co.* v. *National Labor Relations Board*, 326 U. S. 376, does not exist, and this case falls squarely within the principle applied in *Marshall Field & Company* v. *National Labor Relations Board*, 318 U. S. 253; and *National Labor Relations Board* v. *Seven-Up Bottling Co.*, 344 U. S. 344. And as we have also noted in our main brief, pp. 24–25, the fact that this is a rate case, in which Colorado challenges the "end result" of the rate set by the Commission, does not change the rule.

CONCLUSION

For the foregoing reasons, and those set out in our main brief, the judgment of the court below should be reversed to the extent that it invalidates the condition pursuant to which the Commission excluded from cost of service Colorado's losses from the gasoline operations.

Respectfully submitted.

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The Court below reversed because of a fundamental error of law committed by the Commission. An adequate rate of return is a fundamental right which must be awarded in order to avoid confiscation of property. This Court has determined that such a rate must be one that will enable a company to operate successfully, maintain its financial integrity, attract capital and compensate the investors for assumed risks. *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U. S. 591, 605 (1944). The Commission purported to allow Colorado a rate of return of 5¾%.[3] However, from this rate of return calculated to give the company $3,280,317 (R. 125), the Commission deducted $87,202 (R. 115, 198). What the Commission did could otherwise be stated as a deduction from Colorado's legitimate operating expenses. Regardless of how the matter is considered, the effect is the same. Since the Commission allowed the rate of return on a "bare bones" cost of money basis any deduction from return is confiscatory, and since expenses must be allowed as part of the composition of rates (see *Mississippi River Fuel Corporation* v. *Federal Power Commission*, 163 F. 2d 433, 437 (D. C. Cir. 1947)) the deduction in either event was improper.

The situation leading to the deduction which the Court below would not allow arises from the peculiar background circumstances of this case—*i.e.*, the consideration for the transfer of stock incident to the merger which was the subject of the precedent certificate proceedings. No amount of discussion can vary this fact.[4]

[3] Whether that rate was properly allowed or not is the subject of one of the questions in the cross-petition in No. 777.

[4] Additionally, the issue decided adversely to the Commission below will probably be of importance to this one case alone and will not materially affect future rate determinations even relating to Colorado. This is so because the Commission on April 15, 1954 adopted its Opinion No. 269 (*In re Panhandle Eastern Pipe Line Company, et al.*, not yet reported), wherein it treated hydrocarbon

The Commission, however, asserts that the Court below invaded the area reserved exclusively for administrative determination. The Commission attempts to indicate a delicacy involved in such area with broad implications by pointing out that other Federal statutes provide for review of administrative action. Recognizing that there are limits upon authority to reverse upon judicial review of administrative action, it has never been held that a reviewing court cannot reverse where confiscation arises as a matter of law. The area of delicacy must arise in determinations of fact or determinations in which the agency is better qualified to decide technical questions involved. See Davis, *Administrative Law*, §248, pp. 893-897.

The reversal by the Court below cannot have an importance in "the delicate area of judicial review of administrative action". The Court laid bare a plain and fundamental error of law and having done so properly reversed the Commission's action. It is significant that the Commission in its petition here does not assert that the Court below erred in holding that the certificate condition was ineffective in the rate proceeding from the standpoint of substantial justice. The only challenge is to the asserted fact that the Court did not blind itself to the error of law.[5]

extraction operations as non-jurisdictional business except to the extent that such extraction is necessary to the preparation of gas for pipe line transportation.

[5] The Commission in its petition (fn. 8, p. 19) contends that the exclusion of the hydrocarbon expenses from the cost of service represented an appropriate "balancing of the investor and consumer interests". This, of course, does not answer the plain principle used by the Court below that there cannot be a confiscatory order. The Commission recites that during the pendency of the rate proceedings a public offering of Colorado's stock was oversubscribed. This, of course, is completely immaterial not only because the offer of stock was made prior to the rate determination but also because the reasonableness of the "end result" and the allowance of a proper return and legitimate expenses should not be governed by this isolated and unrelated instance.

2. *The question of excluding legitimate costs or reducing the return was before the Commission and the Court.* The deduction made by the Commission was a total amount of $878,202 made up of $421,537 of calculated loss and $456,665 of a computed income tax credit which the Commission claimed would inure to Colorado because of such loss (R. 115, 198). This total exclusion from Colorado's return on expenses was objected to on rehearing (R. 148-153, 169-174, 176-178) and also in its petition for review to the Tenth Circuit (R. 6-7). The lesser amount was objected to on the basis of the allocation adopted by the Commission. The larger amount, on account of the calculated income tax credit, was objected to as a reduction of return. Colorado even showed by a table of simple mathematical calculation (R. 177) that if income taxes were calculated on the orthodox basis (i. e., the taxes associated with the return allowed) that Colorado would be entitled to $642,264 as taxes, whereas the Commission allowed only $185,599 for Federal income taxes (R. 125). This allowance by the Commission when added to the asserted income tax credit of $456,665 gives the tax which should have been associated with the return. In its opinion following Colorado's petition for rehearing the Commission treated the calculated loss and the calculated income tax credit as both coming within the terms of the certificate condition (R. 197-198).[6] The treatment as a matter of principle therefore was before the Commission and the Court.

[6] The Commission stated the following:

"Colorado alleges that it has been deprived of the rate of return to which it is entitled by reason of our treatment of the loss on gasoline operations in computing income taxes. Colorado claims the federal income tax allowance is properly calculated at $642,264, whereas our allowance is $185,599, or a difference of $456,665. (Footnote continued, opposite page.)

SUPREME COURT, U.S.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. 45

FEDERAL POWER COMMISSION,
Petitioner,

v.

COLORADO INTERSTATE GAS COMPANY,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT.

BRIEF OF COLORADO INTERSTATE GAS COMPANY IN OPPOSITION.

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In addition to the foregoing facts which show that the issue of a reduction in return on account of the certificate condition was before the Commission, the validity of that condition was argued before and considered by the Commission during the course of the certificate case, as set forth in the statement above (R. 643-644 fn. 2, 3). This fact of prior opportunity for consideration in itself satisfies any policy which might still remain requiring specification of errors. Any remaining limitation on review is required to give emphasis to a salutary policy of affording an agency the opportunity to consider on the merits those questions which will be urged on review. *National Labor Relations Board* v. *Cheney California Lumber Company*, 327 U. S. 385, 389 (1946); *Marshall Field & Company* v. *National Labor Relations Board*, 318 U. S. 253, 256 (1943); *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143 (1946). These cases, along with others, have been cited by the Commission in support of its petition. The short answer is that the cases are inapplicable to the Commission's contentions because the policy announced in them has been satisfied here.

There is also cited on behalf of the Commission *Panhandle Eastern Pipe Line Company* v. *Federal Power Com-*

"The difference between the claimed income tax liability and the income tax allowance we provided is the result of our treatment of the loss on gasoline operations of $421,537. We have found that the loss on gasoline operations should not be considered a part of the cost of service and with this finding Colorado does not take issue. Colorado would have us compute its federal and state income tax liabilities on the basis of earnings which do not reflect a reduction in the cost of service of the $421,537. To accede to Colorado's contention, however, is to nullify the removal of the $421,537 from the costs which the customers of Colorado should bear. For under Colorado's claim the $421,537 denied it as recovery of a loss on gasoline operations would be recovered in substantial part from the customers in the guise of a reimbursement for a higher tax liability only part of which would in fact be incurred."

mission, 324 U. S. 635 (1945). That case did not involve a problem of reduction in return by the device of not allowing all properly incurred costs. Additionally, that case preceded the Administrative Procedure Act which enlarges a reviewing court's obligation to inspect the whole record. This enlarged power of a reviewing court is considered below.

The Commission also cites *United States* v. *Hancock Truck Lines, Inc.*, 324 U. S. 774 (1945). This case involved an acquiescence to a restriction of routes of a truck line in a certificate order. This again was not so fundamental as a disallowance of proper expenses resulting in a reduction of return. Acquiescence in the denial of fundamental or organic rights is without effect. *Southern Pacific Company* v. *Denton*, 146 U. S. 202 (1892).

The cases cited by the Commission did not have in them the peculiar applicable facts which are of importance here.

3. *The Court had authority to consider the effect of the deduction on the end result.* Colorado contends, as set forth above, that the Court had the authority which it exercised by reason of the fact that the question on exclusion of legitimate costs under the certificate condition was before the Court and had been urged before the Commission. This in itself would clothe the Court with the authority which it exercised.

Even if it be assumed that the point was not properly urged before the Commission and the Court, nevertheless there was authority to remand. The Commission concedes in its petition (p. 13) that a court of appeals has inherent power *vis a vis* district courts to consider and correct errors *sua sponte*. The Commission asserts, however, that it is different where a court of appeals is reviewing an order of an administrative agency properly before it when

INDEX.

	PAGE
OPINIONS BELOW	1
JURISDICTION	1
QUESTION PRESENTED	2
STATUTES INVOLVED	2
STATEMENT	4
ARGUMENT	7
1. The Court made a simple and proper legal determination	7
2. The question of excluding legitimate costs or reducing the return was before the Commission and the Court	10
3. The Court had authority to consider the effect of the deduction on the end result	12
4. There is no collateral attack upon the Commission's certificate determination	15
CONCLUSION	16

there is even a fundamental error of law amounting to confiscation. Bearing in mind that the Commission in its petition nowhere asserts that the deduction which the Court would not allow was proper, the assertion of the Commission is startling. The assertion of the Commission does not give proper effect to the Administrative Procedure Act. Under Section 10(e) of that Act (60 Stat. 237, 5 U. S. C. §1009(e)) it has been held (*Pittsburgh Steamship Company* v. *National Labor Relations Board*, 180 F. 2d 731 at 736, 737 (1950)) that:

> "The reviewing court is required to hold unlawful and set aside agency action, findings, and conclusions not in accordance with law and unsupported by substantial evidence, and in making its determination it is also required to review the whole record. These mandatory provisions define and make specific the requirements of judicial review and extend them beyond the requirements of the Wagner Act."

and further held:

> "We therefore proceed to inquire, upon a consideration of the whole record, whether the order sought to be enforced is supported by the reliable, probative, and substantial evidence and is in accordance with law."

The Commission would have a court vary this plain duty to review the whole record, even where the Court discerns confiscation, solely on the basis that the preamble to Section 10(e) explicitly provides that the review provisions there set forth are inapplicable where "statutes preclude judicial review". The Commission would have this Court believe that such preamble means that the limitation expressed in Section 19(b) of the Natural Gas Act (52 Stat.

Citations.

Cases:

	PAGE
Federal Power Commission v. *Hope Natural Gas Company*, 320 U. S. 591	8, 14, 16
Federal Power Commission v. *Idaho Power Company*, 344 U. S. 17	16
Hormel v. *Helvering*, 312 U. S. 552	14
Marshall Field & Company v. *National Labor Relations Board*, 318 U. S. 253	11
Mississippi River Fuel Corporation v. *Federal Power Commission*, 163 F. 2d 433	8
National Labor Relations Board v. *Cheney California Lumber Company*, 327 U. S. 385	11, 15
Niagara Mohawk Power Corporation v. *Federal Power Commission*, 202 F. 2d 190	15
Panhandle Eastern Pipe Line Company, et al., In re, FPC Opinion No. 269	8
Panhandle Eastern Pipe Line Company v. *Federal Power Commission*, 324 U. S. 635	11, 12
Pittsburgh Steamship Company v. *National Labor Relations Board*, 180 F. 2d 731	13
Rochester Telephone Corporation v. *United States*, 307 U. S. 125	16
Southern Pacific Company v. *Denton*, 146 U. S. 202	12
Unemployment Compensation Commission v. *Aragon*, 329 U. S. 143	11, 15
United States v. *Hancock Truck Lines, Inc.*, 324 U. S. 774	12
United States v. *Tucker Truck Lines, Inc.*, 344 U. S. 33	15

Statutes:

PAGE

Administrative Procedure Act (60 Stat. 237, 5 U. S. C. §1001 *et seq.*)

Section 10 ..... 3, 14

Section 10(e) 3, 7, 13

Natural Gas Act (52 Stat. 821, 15 U. S. C. §717 *et seq.*)

Section 19(a) 2

Section 19(b) 2, 7, 13

Miscellaneous:

Davis, *Administrative Law*, §248, pp. 893-897..... 9

Senate Document No. 248

House Judiciary Committee Report, p. 275.... 14

Senate Judiciary Committee Report, pp. 36, 212 14

IN THE

Supreme Court of the United States

OCTOBER TERM, 1953

No. 710.

FEDERAL POWER COMMISSION,

Petitioner,

v.

COLORADO INTERSTATE GAS COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT.

BRIEF OF COLORADO INTERSTATE GAS COMPANY IN OPPOSITION.

Opinions Below.

The original opinion of the Court of Appeals (R. 593-610) is reported at 209 F. 2d 717; its opinion on rehearing (R. 630-633) is reported at 209 F. 2d 732. The opinion and order of the Federal Power Commission reducing rates (R. 77-140) are reported at 95 PUR(NS) 97.

Jurisdiction.

The original judgment of the Court of Appeals was entered on October 29, 1953 (R. 610). Pursuant to the Federal Power Commission's timely petition for rehearing, the Court of Appeals on December 8, 1953 vacated its

original judgment and granted rehearing (R. 621). The judgment on rehearing was entered on January 25, 1954 (R. 633). The jurisdiction of this Court has been invoked by Petitioner under 28 U. S. C. 1254(1), and Section 19(b) of the Natural Gas Act (15 U. S. C. §717r (b)).

Question Presented.

Whether, in a review of a rate reduction order entered under the Natural Gas Act, the Court below was foreclosed from considering the validity of a contingent rate condition, imposed in previously granting a certificate of convenience and necessity, which had the effect in the instant case of excluding certain expenses in determining the rates ordered by the Commission, when in such previous certificate proceeding the invalidity of that condition was urged and considered by the Commission, and when the Company on asking for rehearing of the instant rate order, and in its petition for review challenged the deduction on two bases: First, that the method of calculating the expenses was not supported by substantial evidence; and, second, that an associated deduction made by the Commission from allowed income taxes amounted to a confiscatory reduction of the cost of service.

Statutes Involved.

1. Section 19 of the Natural Gas Act (52 Stat. 821, 831, 15 U. S. C. 717r) provides in pertinent part:

> (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State, municipality or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. * * *

No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing a written petition praying that the order of the Commission be modified or set aside in whole or in part. * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

2. Section 10 of the Administrative Procedure Act (60 Stat. 237, 243, 5 U. S. C. §1009) provides in pertinent part:

Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion——

* * * * * *

(e) SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not

in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of the agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

Statement.

Early in 1950 Colorado Interstate Gas Company and an affiliate (Canadian River Gas Company) requested the Commission to grant a certificate of convenience and necessity to merge, with Colorado as the surviving corporation then to operate properties of Canadian (R. 564). This merger was necessary to enable Colorado to finance the construction of needed facilities to meet growing public market demands. As consideration for the acquisition of the stock of Canadian, it was proposed that certain liquid hydrocarbon components of natural gas (generally referred to as "natural gasoline") in the gas reserves belonging to Canadian would be conveyed in place to a nominee of Canadian's parent. Colorado was to produce and gather these hydrocarbons in the stream of its gas destined for market and extract them. For this, Colorado was to receive 50% of the gross proceeds from the sale of such hydrocarbons (R. 554). It had been the practice of the Commission to credit to expenses the income derived from these liquid constituents in setting rates. Fear was

expressed by some interested parties that this 50% of gross would not compensate for the work which Colorado was obligated to perform and that any deficiency would be charged to rate payers. As a result, a proposal was first suggested by the City and County of Denver to which Colorado lent its assistance (R. 654-657) and resulted in a condition in the certificate order in the following terms (R. 566-567):

> "* * * if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pursuant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers."[1]

In the course of the Commission's consideration of the certificate case, its counsel stated unequivocally that such a condition would not be enforceable (R. 643-644, fn. 3) and, in addition, in its deliberations the validity of such condition was considered by the Commission since a dissenting Commissioner stated:

> "* * * Should Colorado fail to earn a fair return in the future, then natural gasoline revenues given

[1] The opinions and order in this certificate case are fully reported in 10 FPC 105 (1951).

> up to Southwestern cannot be treated as revenues of Colorado. * * * I question seriously whether the stockholders of Colorado can be compelled to accept a confiscatory rate of return simply because of a condition inserted in a certificate by the Federal Power Commission and accepted by their present Board of Directors." (R. 643, fn. 2).

Subsequent to the issuance of this certificate, the Commission embarked upon hearings in a rate investigation against Colorado which was originally instituted in 1948. These rate proceedings resulted in an order adopted July 31, 1952 and issued August 8, 1952 directing Colorado to reduce its rates on sales for resale in interstate commerce by approximately $3,100,000 per year.[2] Reflected in this ordered reduction was $878,202 because of a loss which the Commission concluded came within the terms of the certificate condition. This $878,202 deduction from Colorado's return was made up of $421,537 which the Commission found to be the excess of expenses over income on the liquid hydrocarbon operations, plus an income tax credit on account of such expenses in the amount of $456,665 (R. 115, 198). Colorado had alleged as error in its petition for rehearing addressed to the Commission and in its petition for review to the Court below that such deduction should not be made. As to the $421,537 of the Commission-found loss, Colorado contended that there was not substantial evidence to support such finding (R. 6, 148-153, 169-174). As to the deduction of $456,665 on account of an alleged income tax credit, Colorado contended that such deduction was not within the terms of the certificate condition and amounted to a deduction from its allowed rate of return—reducing

[2] The petition for certiorari on behalf of the Commission states that this amount was about $2,703,000. The ordered reduction, however, was expressly found to be $3,100,000 (R. 139).

the return from 5½% purported to be allowed to an actual 5.10% (R. 6-7, 153, 176-178).

The Court below in the review proceeding instituted by Colorado pursuant to Section 19(b) of the Natural Gas Act (52 Stat. 821, 831, 15 U. S. C. §717r(b)) found that the Commission's method of determining the loss of $421,537 was supported by substantial evidence (R. 630-631). The Court did not expressly deal with the assertion of Petitioner that the alleged income tax credit made by the Commission under the certificate condition amounted to an invalid deduction from allowed return. The Court did, however, unanimously hold that the certificate condition was ineffective as a means of reducing the rate of return to which Colorado was found to be entitled.

The Commission petitioned for rehearing asserting that Colorado had not attacked the validity of the certificate condition. The Court granted rehearing (R. 621) and after full briefing and further argument reaffirmed its former position (R. 630-633). In its reaffirmance, the Court noted that Colorado did object to the exclusion of the asserted loss on hydrocarbon extraction operations. The Court also placed its treatment of the reduction of return upon its power to correct a fundamental error *sua sponte* and upon Section 10(e) of the Administrative Procedure Act which requires review of the whole record, as well as the Court's duty to determine whether the end result of the Commission's rate order was fair.

Argument.

1. *The Court made a simple and proper legal determination.* The Commission in its petition attempts to create an aura of broad importance and impact in its issue in the instant case which simply does not exist.

INDEX.

	PAGE
Opinions Below	1
Jurisdiction	2
Question Presented	2
Statutes Involved	3
Statement	3
Summary of Argument	12
Argument	15
I. Upon the whole record, and under the peculiar facts of this case, the question was before the Court of Appeals	15
A. It was objected by Colorado that no loss should be calculated or deducted	16
1. The $421,537—Objections to Method etc.	16
2. The $456,665—Objection that allowed rate of return was reduced	16
B. The Commission fused the questions of calculated loss and income tax credit as being one and the same	17
C. The Commission was apprised that a contention would be made on a reduction of return because of the gasoline deduction	18
1. Notice to the Commission	18
2. The law does not support the Commission	20
II. There were reasonable grounds to excuse the failure to raise the question	21
A. The Commission already had considered the issue	21

PAGE

B. This previous consideration satisfied the policy of Section 19(b) 22

C. The nature of the question is excuse for failure to raise 23

1. The public interest 23

2. The fundamental importance of the issue 26

III. The Court of Appeals did not upset the Commission's certificate determination in the merger case but merely exposed an error of law 27

IV. The Administrative Procedure Act justified the court below in considering the question 32

CONCLUSION 37

APPENDIX 38

TABLE OF CASES.

	PAGE
Addyston Pipe & Steel Company v. *United States*, 175 U. S. 211 (1899)	24
American Power & Light Company v. *Securities and Exchange Commission*, 141 F. 2d 606 (1st Cir. 1944)	27
Bingham's Trust v. *Commissioner of Internal Revenue*, 325 U. S. 365 (1945)	31
Colorado Interstate Gas Company, In the Matter of, 10 F. P. C. 105 (1951)	23
Federal Power Commission v. *Hope Natural Gas Company*, 320 U. S. 591 (1944)	24, 26, 31
Federal Power Commission v. *Idaho Power Company*, 344 U. S. 17 (1952)	14, 27
Federal Power Commission v. *Pacific Power & Light Company*, 307 U. S. 156 (1939)	28
Heikkila v. *Barber*, 345 U. S. 229 (1953)	34, 35
Helvering v. *Wood*, 309 U. S. 344 (1940)	26
Louisville & Nashville Railroad Company v. *Mottley*, 219 U. S. 467 (1911)	24
Marshall v. *Pletz*, 317 U. S. 383 (1943)	12, 15
Marshall Field & Co. v. *National Labor Relations Board*, 318 U. S. 253 (1943)	21
May Department Stores Company v. *National Labor Relations Board*, 326 U. S. 376 (1945)	12, 20, 21
National Labor Relations Board v. *Cheney California Lumber Company*, 327 U. S. 385 (1946)	36
National Labor Relations Board v. *Pittsburgh Steamship Company*, 340 U. S. 498 (1951)	36
National Labor Relations Board v. *Seven-Up Bottling Company*, 344 U. S. 244 (1953)	21
Niagara Mohawk Power Corporation v. *Federal Power Commission*, 202 F. 2d 190 (D. C. Cir. 1952), affirmed, 347 U. S. 239 (1954)	31

PAGE

Panhandle Eastern Pipe Line Company, 3 P. U. R. 3d 396 (1954) 4

Pittsburgh Steamship Company v. *National Labor Relations Board*, 180 F. 2d 731 (6th Cir. 1950) 36

Rochester Telephone Corporation v. *United States*, 307 U. S. 125 (1939) 31

Transcontinental Gas Pipe Line Corporation, In the Matter of, 94 PUR (NS) 333 (1952) 17

Unemployment Compensation Commission v. *Aragon*, 329 U. S. 143 (1946) 13

United States v. *Ballard*, 322 U. S. 78 (1944) 15

United States v. *Hancock Truck Lines, Inc.*, 324 U. S. 774 (1945) 26

United States v. *Tucker Truck Lines, Inc.*, 344 U. S. 33 (1952) 13, 25, 26, 27

STATUTES.

Administrative Procedure Act, 60 Stat. 237, 5 U. S. C. §§1001 *et seq.* 3

Section 10 ..... 14, 32, 33, 34, 36, 38

Section 10(e) 15, 20, 33

Immigration Act of 1917, 39 Stat. 889 34

Section 19 33

Labor Management Relations Act, 61 Stat. 136, 29 U. S. C. §§151 *et seq.* 20

Section 10(e) 20

Natural Gas Act, 52 Stat. 821, 15 U. S. C. §§717 *et seq.* 2, 3, 38

Section 1(a) 23

Section 5(a) 3, 24

Section 7 3

Section 19 33

Section 19(b) 2, 14, 20, 21, 22, 23, 32, 34

Other Authorities Cited.

	PAGE
Senate Document No. 248 (79th Cong. 2d Sess.)	33, 35
House Judiciary Committee Report	33
House Proceedings	33, 35
Senate Judiciary Committee Report	33, 34
Senate Proceedings	34, 35
Restatement of the Law, Contracts, §306	22
Comment a	22
Williston on Contracts (rev. ed. 1936), §698A	22

831, 15 U. S. C. §717r(b)) precludes the review prescribed by the Administrative Procedure Act. This plainly is not the intent.

In the first place, a reading of that Section clearly indicates that there is a broader implication, *i.e.*, the review provision of the Administrative Procedure Act is not applicable if review in its entirety is withheld. The Senate Judiciary Committee recognized that: "the rule of review stated is that which is judicially recognized" (Sen. Com. Rep., Sen. Doc. No. 248, p. 36). Also, the Senate Judiciary Committee stated in regard to this limitation: "Very rarely do statutes withhold judicial review" (*Id.* p. 212). In the report of the House Judiciary Committee, it was stated under Section 10: "This section requires adequate, fair, effective, complete, and just determination of the rights of any person in properly invoked proceedings". (*Id.* p. 275). It is appropriate, therefore, to determine the Court's authority in the terms of "that which is judicially recognized".

Judicially it had been recognized prior to the enactment of the Administrative Procedure Act that there always are exceptional cases or circumstances which will prompt an appellate court to consider questions of law which were not pressed upon the court or the administrative agency below if injustice might otherwise result. *Hormel* v. *Helvering*, 312 U. S. 552, 557, 559 (1941). The effect of Section 10 of the Administrative Procedure Act would appear to give courts on review the same authority that such courts have *vis a vis* district courts where plain error on a question of law not involving administrative expertise is laid bare.

This authority of an appellate court in a case like the instant one is additionally fortified by the fact that since *Federal Power Commission, et al.* v. *Hope Natural Gas Company*, 320 U. S. 591 (1944), a reviewing court's concern

is with the "end result" of the rate determination. The obligation of a reviewing court in such a proceeding is to determine whether an order viewed in its entirety meets the requirements of the Natural Gas Act. The Court below discharged that obligation.

The Commission cites numerous cases in an attempt to support its petition. Most of these cases are not applicable here because the administrative agency in the instant case did consider the validity of the certificate condition. This distinguishing feature certainly applies to *National Labor Relations Board* v. *Cheney California Lumber Company*, 327 U. S. 385 (1946) and *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143 (1946). Additionally, most cases cited antedate the Administrative Procedure Act. The Commission asserts, however, that the principle which it is striving to establish had been applied by this Court subsequent to the Administrative Procedure Act and cites *United States* v. *Tucker Truck Lines, Inc.*, 344 U. S. 33 (1952). *Tucker* is clearly distinguishable because there was involved in that case merely a procedural defect to which no objection was made in the administrative proceedings. As this Court recognized in *Tucker*, a procedural irregularity requires prompt objection to avoid waiver. The plain fact is that in instant case the Court below did not abuse its appellate or reviewing authority.

4. *There is no collateral attack upon the Commission's certificate determination.* The Commission in the last portion of its petition indicates that the Court below leaves the certificate standing without the condition and Colorado did not seek review of this certificate case. It is a well recognized doctrine that *res judicata* and estoppel do not apply to administrative proceedings. *Niagara Mohawk Power Corporation* v. *Federal Power Commission*, 202 F. 2d 190 (D. C.

Cir., 1952, affirmed 347 U. S. 239 (1954)). Additionally, the offending certificate condition probably could not have been made the subject of previous judicial review had Colorado been dissatisfied with it. The merger condition related to rates and did not of itself adversely immediately affect Colorado, but would affect the company only on the contingency of future administrative action, *i.e.*, a rate case. Review under such circumstances is premature. *Rochester Telephone Corporation* v. *United States*, 307 U. S. 125, 130 (1939) and *Federal Power Commission* v. *Hope Natural Gas Company*, *supra*, at 619.

The Court below has done nothing but strike down the condition as an instrument for reducing the proper cost of service in this rate case. It has in no way attempted to affect the status of the Commission's issued certificate of convenience and necessity as was done in *Federal Power Commission* v. *Idaho Power Company*, 344 U. S. 17 (1952) which the Commission cites. The Commission is still free to do whatever it may under its certificate authority.

Conclusion.

The decision of the Court below is plainly correct to the extent the Commission has attacked it here. That Court discharged its duty upon review not only because the issue in principle was raised before the Commission, had previously been considered by the Commission, and was raised before the Court, but also because of the discharge of the Court's expanded review responsibility under the Administrative Procedure Act and the doctrine of the *Hope* case. It is, therefore, respectfully submitted that the petition for certiorari filed on behalf of the Commission should be denied as lacking in importance and substance. Also the

writ should be denied for failure to disclose or even assert error in the substantive determination below which prevents a confiscatory end result.

Respectfully submitted,

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May, 1954.

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SUPREME COURT, U. S.

No. 45.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1954.

FEDERAL POWER COMMISSION,
Petitioner,

v.

COLORADO INTERSTATE GAS COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR COLORADO INTERSTATE GAS COMPANY.

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> tion in the cost of service of the $421,537. To accede to Colorado's contention, however, is to nullify the removal of the $421,537 from the costs which the customers of Colorado should bear. For under Colorado's claim the $421,537 denied it as recovery of a loss on gasoline operations would be recovered in substantial part from the customers in the guise of a reimbursement for a higher tax liability only part of which would in fact be incurred" (R. 127-128).

Colorado filed its petition to review in the court below. *Inter alia*, it was alleged that the Commission should not have made any deduction for alleged loss in gasoline operations. Also, it was asserted that in any event the calculated tax credit amounted to a confiscatory reduction in the rate of return (R. 7).

The court below decided that the elimination of the gasoline loss was wrong. In so deciding the court stated:

> "It would seem that the elimination of the loss of the gasoline operations from the cost of service deprives Colorado of earning the fair rate of return to which it is entitled. It means that this loss must come out of the net profits of the stockholders notwithstanding that it is an element of cost of service. Nor is it an answer to say that this was a condition of the merger order and that, therefore, Colorado's stockholders are bound and saddled with this loss. We are dealing here with a business affected with a public interest. Parties in such businesses are not free to contract as they choose. They are subject to regulation by proper Governmental authority. In the exercise of its jurisdiction, such authority must be fair, both to the public and to the utility. It is the statutory duty of the Commission to establish on the one hand rates that are fair and just to the utility and on the other hand to strike down rates that

> demand an unlawful and unreasonable exaction. A rate based upon the exclusion from the cost of service, no matter for what reason, of a substantial amount of admitted operative cost does not and cannot reach a just end result and may, therefore, not stand.
>
> "The provision in the merger order that such operative costs as we are considering here should be eliminated from the cost of service base in subsequent rate hearings does not alter these basic principles. When that proceeding was before the Commission, it was its statutory duty to determine whether the plan was fair and just to Colorado's gas users. If it found that it might result in an unjust burden on them, it had power to disapprove it. It could not predicate its approval thereof upon a condition which it could not adopt in a rate hearing and which would thereafter deprive Colorado of the opportunity to earn a fair return upon its 'investment'" (R. 271, 209 F. 2d 727).

The court then recognized that this would require further consideration of the income tax allowance (R. 277).

Upon rehearing, the court below noted that Colorado had objected to the exclusion of the calculated loss on gasoline operations, although the objection was not placed upon the legal ground used by that court (R. 300). Aside from that, the court concluded that it could correct manifest error which deprived Colorado of a fair return (*id.*). The court also premised its conclusions upon its obligation to examine the "end result" and upon its expanded review responsibility under Section 10 of the Administrative Procedure Act.

Summary of Argument.

The issue here relates only to the authority of the Court of Appeals to deal with the question of reducing the rate of return. That authority may be sustained by any meritorious ground. *Marshall* v. *Pletz*, 317 U. S. 383 (1943).

I. The record facts show that the issue was raised in the rate proceeding, both as to the calculated loss and the associated income tax credit. As to the former (making up $421,537 of the deduction) Colorado objected before the Commission and in the court below to the method used and asserted a lack of substantial evidence to support that deduction. On the latter, the tax credit ($456,665), specific objection was made that this amounted to a reduction in the rate of return—the ground used by the court below in reversing. Clear reference was made to the Commission and to the court that the effect of the Commission's treatment of a tax credit flowing from the gasoline loss reduced the return which the Commission found reasonable and purported to allow. This the Commission recognized.

Upon rehearing, the Commission decided that the point on reducing the rate of return was not well taken, not because that was not the result, but because the calculated loss required this greater deduction. The Commission considered the two deductions to be required under the merger condition and dealt with them as parts of a whole.

The Commission was therefore apprised that a reduction in return would be challenged. By the Commission's own action both the loss and tax credit were treated as the same so far as the propriety of making the deduction was concerned. It was apprised, therefore, of the issue upon which the court below acted. *May Department Stores Company* v. *National Labor Relations Board*, 326 U. S. 376 (1945).

II. If the question was not before the Court of Appeals, then the peculiar facts excuse the failure to raise the question.

The Commission had the question of the enforceability of the condition very forcibly brought to its attention in the previous interrelated certificate case. The Commission's own counsel and a dissenting Commissioner stated their doubts as to the condition's validity. The Commission acted with this knowledge in mind.

This previous assertion of possible invalidity satisfies the policy of statutes such as the Natural Gas Act which limit review to objections raised. This policy is that an agency should have the opportunity to consider the matter and make its decision. *Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143, 155 (1946). Here the Commission had that opportunity in the certificate proceedings.

Also, the matter of reducing a reasonable rate of return involves a fundamental right. Since Colorado's business is affected with a public interest it cannot, by agreement to the condition, prejudice either consumer or investor interests. Being a fundamental and not merely a personal right involved, there was no effective waiver of a reasonable rate of return. See *United States* v. *Tucker Truck Lines, Inc.*, 344 U. S. 33 (1952).

III. The court below did not in any way interfere with the Commission's administrative function. The Commission claims that the court did so because it left the merger stand without the condition. This certainly is not true for the Court of Appeals gave no direction to the Commission on the certificate nor can any such direction be implied. It merely laid bare the Commission's error of law and instructed that its opinion should be followed in the rate

determination. The Commission is unfettered by any judicial requirement so far as the certificate is concerned. This is fully consistent with a court's authority upon review. *Federal Power Commission* v. *Idaho Power Company*, 344 U. S. 17, 20 (1952).

The court below dealt with the legal question: can a proper rate of return be reduced under the aegis of a condition to a certificate? There has been no interference with the Commission's factual expertise.

The rate condition of the certificate order was by its terms only contingently effective, and in any event was not *res judicata*. There could have been no review at that time, and subsequent review cannot be denied on the basis of collateral attack. The lack of review of the condition at that time, therefore, is immaterial.

IV. The court below recognized a greater responsibility upon review by virtue of Section 10 of the Administrative Procedure Act. The Commission denies this expanded responsibility and contends that Section 19(b) of the Natural Gas Act, standing alone, is what controls; but its reasons for arguing that Section 10 should be ignored are unsound. In particular, the introductory clause of Section 10 of the Administrative Procedure Act denying review where "statutes preclude judicial review" does not apply to where review is limited, as the Commission contends, but only to where any review is denied.

The court below properly discharged its responsibility upon review and in support of its action properly recognized its power under all of the law—including its broadened responsibility under that remedial legislation.

ARGUMENT.

The only issue here is whether the Court of Appeals *could* consider the question—not whether it made a proper determination. The Commission in stating the "Question Presented" (Com. Brf. pp. 2-3)[9] unduly narrows the inquiry. The question as presented by the Commission is limited to whether Section 10(e) of the Administrative Procedure Act empowered the court below to reverse under the circumstances of this case. The basic assumption of the Commission is that the court below depended in the main, at least, upon that statutory provision.

The inquiry here is broader. At this juncture, the judgment may be supported by any meritorious ground whether or not urged below. *Marshall* v. *Pletz*, 317 U. S. 383, 390 (1943); *United States* v. *Ballard*, 322 U. S. 78, 88 (1944).

I.

Upon the whole record, and under the peculiar facts of this case, the question was before the Court of Appeals.

The record facts show that the Commission made two important deductions based on a calculated loss on account of the gasoline operations. *First*, there was the deduction of $421,537 on the calculated loss itself (R. 79). *Second*, there was an additional $456,665 deducted from the cost of Colorado's service on account of an alleged credit to Colorado's Federal income taxes on account of that loss (R. 127-128).

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[9] The reference "(Com. Brf. p.....)" will be used in citing Commission's Brief on the merits.

Colorado objected to both of these deductions before the Commission and in its petition for review to the court below.

A. It was objected by Colorado that no loss should be calculated or deducted.

1. The $421,537—Objections to Method etc.

The Commission concedes that Colorado contended that no loss should be found on the gasoline operations—that there was a net profit, not a loss (Com. Brf. pp. 15-16).[18] While Colorado did not challenge the legal propriety of deducting the calculated loss on this specific amount of $421,537, there can be no doubt whatsoever that it did contend that the deduction was improper under the Commission's calculation or allocation method. Objections went to contentions in regard to the method, the failure to use the appropriate factors under the adopted method, the lack of substantial evidence to sustain the conclusion that there was a loss, and to the contention that the method adopted violated the certificate condition (R. 98-103, 106-114). Similar contentions were made in the court below (R. 7).

It is clear, therefore, that there was submitted to the Commission, and to the Court of Appeals, the contention that no calculated loss should be deducted. That fact cannot be denied, nor is it denied.

2. The $456,665—Objection that allowed rate of return was reduced.

On the calculated so-called Federal income tax credit in the amount of $456,665, Colorado specifically objected

[18] The Commission argues here that "Colorado conceded, that the gasoline operation loss, if properly determined, should be excluded" (Com. Brf. p. 16). Without intending to engage in semantics, Colorado submits that the fairer construction of the record is that the propriety of the deduction was assumed. Colorado certainly felt that the allocation of the costs was erroneous. The Commission Brief makes that clear (Com. Brf., pp. 15-17).

before the Commission that this, alone, had the effect of reducing the rate of return.

Colorado demonstrated by mathematical calculation that this was so (R. 112-114). Colorado also showed that it had been the Commission's uniform policy to allow Federal income tax as a part of the cost of service associated with the rate of return.[11] This, however, was not done in regard to Colorado (*Id.*). The record leaves no doubt of this fact.

The Commission recognized that this point was made when it stated Colorado alleges that it has been deprived of the rate of return to which it is entitled by reason of our treatment of the loss on gasoline operations in computing income taxes (R. 127).

Admittedly, therefore, the Commission had before it (R. 127), and the court below had before it (R. 7) an objection that the Commission's treatment to this extent amounted to a reduction of the rate of return.

B. The Commission fused the questions of calculated loss and income tax credit as being one and the same.

After Colorado applied to the Commission for rehearing of the rate reduction order, the Commission issued a short opinion (R. 118-130). In this opinion, dealing with the objections raised in an application for rehearing filed pursuant to Section 19 of the Natural Gas Act, the Commission considered the calculated gasoline operation loss and a calculated associated tax saving as being parts of a whole.

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[11] The Commission has stated this policy (Re *Transcontinental Gas Pipe Line Corporation*, 94 PUR (NS) 333 at 351 (1952)):

> "It has been our consistent practice to allow in the Cost of Service, the amount of Federal income taxes which the utility would actually pay to the Government based upon a fair return, adjusted for all tax credits to which the corporation is entitled" (R. 112).

IN THE

Supreme Court of the United States

OCTOBER TERM, 1954

No. 45.

FEDERAL POWER COMMISSION,
Petitioner

v.

COLORADO INTERSTATE GAS COMPANY,
Respondent

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR COLORADO INTERSTATE GAS COMPANY.

Opinions Below.

The original opinion of the Court of Appeals (R. 262-279) is reported at 209 F. 2d 717; its opinion on rehearing (R. 299-302) is reported at 209 F. 2d 732. The opinion and order of the Federal Power Commission reducing rates (R. 47-97) are reported at 95 PUR (NS) 97.[1]

[1] The Commission's opinion and order approving the merger of the properties and facilities of Colorado Interstate Gas Company with those of Canadian River Gas Company (R. 243-261) are reported at 10 F. P. C. 105 *et seq.*

This fusion is clear. The Commission first recognized Colorado's objection that the tax treatment amounted to a reduction in the rate of return. It next stated that the difference between the claimed tax liability and the income tax allowed resulted from the treatment of the calculated loss on gasoline operations. Then the Commission concluded that "To accede to Colorado's contention, however, is to nullify the removal of the $421,537 from the costs which the customers of Colorado should bear" (R. 127-128). The Commission did not deny, nor does it now deny, that the effect of its treatment did reduce the return.

The Commission therefore considered the loss which it calculated, and the associated calculated tax saving as being parts of a whole deduction. It admitted that Colorado objected to the greater part of this whole as being an improper deduction from the rate of return. It then went further and stated that to satisfy Colorado's objection would nullify the whole.[12]

The clear conclusion was that the Commission felt there was presented an objection to a deduction from return on account of the gasoline operations. The Commission dealt with the problem on that basis.

C. The Commission was apprised that a contention would be made on a reduction of return because of the gasoline deduction.

1. Notice to the Commission.

The Commission deals with this point in the comparative obscurity of a footnote (Com. Brf., p. 17, note 6).

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[12] True, the Commission stated "We have found that the loss on gasoline operations should not be considered a part of the cost of service and with this finding Colorado does not take issue" (R. 127). Of course, Colorado did take issue, as the cited record shows. This statement, however, does not vary the conclusion that the calculated loss and the assumed tax deduction were inseparable parts of one whole item.

Jurisdiction.

The original judgment of the Court of Appeals was entered on October 29, 1953 (R. 279). Pursuant to the Federal Power Commission's timely petition for rehearing, the Court of Appeals on December 8, 1953 vacated its original judgment and granted rehearing (R. 290). The judgment on rehearing was entered on January 25, 1954 (R. 302). The petition for a writ of certiorari was filed on April 23, 1954, and granted on June 7, 1954 (R. 327). 347 U. S. 1009. The jurisdiction of this Court rests upon 28 U. S. C. 1254(1), and Section 19(b) of the Natural Gas Act (15 U. S. C. §717r(b)).

Question Presented.

Whether, in a review of a rate reduction order entered under the Natural Gas Act, the court below was foreclosed from considering the validity of a contingent rate condition, imposed in granting a certificate of convenience and necessity, (which had the effect in the instant case of reducing the rate of return by excluding certain expenses in determining the rates ordered by the Commission), when (i) in such previous certificate proceeding the invalidity of that condition was urged before and considered by the Commission, and (ii) when the Company on asking for rehearing of the instant rate order, and in its petition for review objected to the deduction on two bases:

> First, that no deduction should be made because the method of calculating the expenses was not supported by substantial evidence; and,
>
> Second, that an associated deduction made by the Commission from allowed income taxes amounted to a confiscatory reduction of the rate of return; particu-

There can be no doubt that Colorado's contention in relation to an unwarranted reduction of the purported rate of return allowance was serious. Colorado presented to the Commission a clear mathematical calculation based upon record facts to show that its return was being reduced below what the Commission claimed to allow. This calculation and the associated discussion of the claimed error occupies more than one and one-half pages of the printed record here (R. 112-114) and is the subject of the treatment of a specification of error which noted that the Commission's action reduced the rate of return below the 5¾% found to be reasonable (R. 103).

The Commission, however, declares that this did not apprise it that the validity of the merger condition was being challenged (Com. Brf., p. 17, note 6). Colorado submits that the facts did apprise the Commission. Colorado, after describing the error and showing its departure from valid regulatory practice, said "The action of the Commission in this regard, therefore, is arbitrary, capricious, discriminatory and highly prejudicial to Colorado" (R. 113-114).

Bearing in mind that the Commission is not here seriously challenging the correctness of the determination below (and under the question as presented, could not do so), it is appropriate to analyze exactly what the court below did. Basically, it was held that the gasoline elimination deprived Colorado of "earning the fair rate of return to which it is entitled" (R. 271). This is exactly the point Colorado raised in discussing the associated tax credit. The Commission considered the gasoline loss and the tax credit as parts making up the whole of the deduction from return.

larly when the Commission considered both deductions to involve the same principle.

Statutes Involved.

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U. S. C. §717 *et seq.*, and of the Administrative Procedure Act, 60 Stat. 237, 5 U. S. C. §1001 *et seq.*, are set forth in the Appendix, *infra*, pp. 38-39.

Statement.

The question before the Court arises out of two proceedings before the Commission which turned out to be interrelated.

In the first, the Commission in 1948 instituted a rate investigation against Colorado Interstate Gas Company[2] under Section 5(a) of the Natural Gas Act (R. 9-11). Hearings on this started October 1, 1951 (R. 11). Between the institution of the investigation and the beginning of hearings therein, the second proceeding arose and was determined.

The second proceeding involved an application filed early in 1950 under Section 7 of the Natural Gas Act by Colorado for a certificate of public convenience and necessity to construct necessary facilities to satisfy public demands and to drill wells at a total estimated cost of $13,500,000. Colorado estimated that it could not finance this necessary work without a merger with Canadian River Gas Company whose stock was 100% held by Southwestern Development Company. Canadian River was a producer of natural gas and sold large quantities to Colo-

[2] Colorado Interstate Gas Company will be referred to as "Colorado", and The Federal Power Commission as "Commission".

2. The law does not support the Commission.

The case authority cited by the Commission to support its position fails to do so in the light of these facts (Com. Brf., pp. 18-19). The Commission likens the restriction of Section 19(b) of the Natural Gas Act to Section 10(e) of the Labor Management Relations Act (formerly Section 10(e) of the National Labor Relations Act). The Labor Act would appear to have a stronger restriction—that Act excuses failure to raise an objection only "because of extraordinary circumstances * * *." The Natural Gas Act excuses failure where there is "reasonable ground for failure so to do * * *" In any event the cases cited by the Commission do not support the proposition that the requirements of Section 19(b) were not met by Colorado's objections. In fact one of the cases cited supports Colorado. The others, by their facts, are distinguishable.

In fact one of the cases cited supports Colorado. The others, by their facts, are distinguishable.

In *May Department Stores Company* v. *National Labor Relations Board*, 326 U. S. 376 (1945) this Court applied the test of whether an "* * * objection was sufficiently specific to apprise the Board of the question now presented * * *" in order to determine the power of the lower court to consider it (326 U. S. at 386, note 5). This Court concluded there that the peculiar circumstances coupled with an objection to an Examiner's intermediate report claiming the same not to be "supported or justified by the record" was sufficient to apprise the Board of the point there involved. Sufficiency of apprisal is, therefore, the test. In the *May Department Stores* case, this Court noted that the objection fell short of desirable specificity but deemed it sufficient in that case. Under the circumstances of this case, like the *May Department Stores* case, the peculiar circumstances cure any lack. Here, there was objection to a

rado. Southwestern had valuable tax advantages arising from its ownership of Canadian stock but would transfer the same to effect the merger in consideration of receiving rights in natural gasoline.[3] Colorado was, in the main, to process the gas and deliver it to Southwestern, and the latter was to give Colorado 50% of gross revenues for performing the production, gathering and extraction functions. Canadian River was a party to this certificate proceeding since the case involved operations of Canadian River over which the Commission had jurisdiction (R. 243-261).

Under Commission rate-making policies then in effect, the revenue which Colorado would have derived from the sale of natural gasoline (or which Canadian River would derive) would have been a credit to operating costs and thus have an effect on reducing rates.[4]

The transfer of the natural gasoline therefore posed a problem. While the Commission felt that there was a good chance that, through the merger, Colorado would realize almost as much in the way of tax benefits as would be given up through the transfer of natural gasoline (R. 252-253), yet some participants felt that the natural gasoline transfer would adversely affect rate payers. A representative of the City and County of Denver, Colorado (an intervener in the certificate case), therefore suggested as a condition to the certificate, an accounting procedure to remove the concern that rate payers would suffer (R. 322-325). Colorado counter-suggested that if the loss through

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[3] This is a generic name applied to certain extractable liquid hydro-carbon fractions which raw natural gas contains in some areas. The product is in demand and is, therefore, a valuable natural gas constituent.

[4] This policy was explained but changed in *Panhandle Eastern Pipeline Company*, 3 P. U. R. 3d 396, 422-424 (1954). The Commission now credits such revenues only if and to the extent that such extraction is necessary to the preparation of the gas for interstate transportation.

reduction in the rate of return because of the treatment of the gasoline operations question. By the Commission's own treatment, the two deductions made from the return were dealt with as concommitant things. The Commission clearly knew, therefore, at the time the objections were made in the application before it for rehearing, what would have to be faced upon review. As in *May Department Stores*, the Commission had made all the findings necessary to permit the reviewing court to deal with the issue.

The other two cases cited (*Marshall Field & Company* v. *National Labor Relations Board*, 318 U. S. 253 (1943); and *National Labor Relations Board* v. *Seven-Up Bottling Company*, 344 U. S. 244 (1953)) exemplify the proposition that very broad objections which do not apprise an agency of fundamental contentions are not sufficient. The circumstances here show apprisal.

Having faced up to the situation, having overruled Colorado's objection that the rate of return was being improperly reduced, the Commission cannot now claim lack of apprisal to mend its error in reducing the rate of return it found to be proper.

II.

There were reasonable grounds to excuse the failure to raise the question.

Assuming at this point that an apprising objection had not been made, Colorado contends that there is reasonable ground for failure to raise the objection and thus the limitation of Section 19(b) does not apply.

A. The Commission already had considered the issue.

Without doubt, the Commission considered the certificate case and the rate case to be interrelated. This is evidenced

the gasoline function exceeded the additional revenues retained because of the tax savings, the net loss would not be charged to the rate payers (R. 325).

The Commission sat *en banc* to hear oral argument on this certificate case and the question again arose as to attaching a condition to the certificate on the gasoline question. The Commission's counsel stated that Colorado's Board could not bind the stockholders to absorb any loss through the gasoline operations over and above what Colorado would receive. One of the Commissioners (of the majority in issuing the certificate) agreed in the course of the oral argument that there would be confiscation if the return got as low as 4% and such condition would not be binding (R. 311-312, note).

Nevertheless, a condition was proposed by Colorado in specific terms related to the Commission's Code of Accounts and specifying that if expenses exceeded revenue, the loss would not be part of the cost of service.[5]

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[5] The proposal was as follows (R. 289-290):

> "If, as a result of carrying out the terms and conditions in the transaction proposed as a part of the merger of Canadian River into Colorado Interstate whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado Interstate is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenue to be received by Colorado Interstate from the operation of the Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the amounts chargeable as Residuals Operation Expenses (Account 747.2) and Residuals Maintenance Expenses (Account 747.3) exceed the amounts to be paid to Colorado Interstate pursuant to said transaction which is accounted for as Residuals Produced (Account 747.1) and Revenue from Processing Natural Gas (Account 617) then and in that case in any proceeding in which the effective or proposed rates of Colorado Interstate are under inquiry the amount by which said expenses exceed the amount so received and accounted for as Residuals Produced and Revenue from Processing Natural Gas shall not be considered as a cost of service."

not only by the fact of the rate condition relating to natural gasoline included in the order granting a certificate, but also by another fact. The Commission majority in its certificate case opinion stated that with the conclusion of the certificate matter, future operations were settled and that, therefore, the rate case should move to a speedy conclusion.[13]

The record shows that the Commission had been confronted by its own counsel with an argument that a certificate condition such as that involved here would not be valid and could be confiscatory (see *supra* p. 5). Also, the dissenting Commissioner raised this very point (R. 311-312, note 10 F. P. C. 133). Given these facts, what would it have availed Colorado to urge before the Commission that the condition was confiscatory *per se* and should not apply?[14]

B. This previous consideration satisfied the policy of Section 19(b).

The facts of this case are most peculiar when one considers the interrelation of the certificate proceedings and

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[13] The Commission's exact words were (R. 255-256, 10 F. P. C. 118):

> "Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investigation should be brought to a speedy conclusion. In our order issued March 1, 1951, we required Colorado, within four months of that date, to report to us the completion of the acquisition, the commencement of operation by it of facilities acquired, and proof of dissolution of Canadian. Therefore, we have, by order entered today, fixed the date of hearing in the rate case for August 1, 1951, which is one month after the required [d]ate for such report."

This August 1, 1951 date was subsequently changed to October 1, 1951 because the mechanics of the merger were not accomplished as speedily as anticipated.

[14] This raises the additional point that the law does not require the doing of a useless act. This has been true from Coke's time. See *Williston on Contracts* (rev. ed. 1936) §698A; *Restatement of*

A majority of the Commission decided the certificate should issue and stated (10 F. P. C. 118-119):

> "A summary of the salient conclusions justified by the facts appearing on this record will demonstrate succinctly the desirability of the project laid before us for judgment:
>
> "(1) The merger can be reasonably expected to cost Colorado no more than $3,762,713 spread over a 23-year period and may result in a cash benefit to it over the same period of $4,376,495.
>
> "(2) Colorado will acquire legal title to physical assets, the original cost of which, after depreciation, is $10,979,522. These include natural gas reserves containing some 3 trillion cubic feet of gas which is expected to be adequate to supply the needs of the gas consumers in the Rocky Mountain area for at least 20 years at a low cost.
>
> "(3) Colorado will gain valuable reversionary rights in the physical assets mentioned above which, but for the merger, would have matured to the benefit of Southwestern rather than Colorado, probably by 1972.
>
> "(4) The corporate structure of the Texas-to-Denver pipeline will be greatly simplified with resulting savings.
>
> "(5) There will be created through the merger a financially sound natural gas company able to finance present and future expansions to meet the needs of the gas consumers dependent upon its system.
>
> "(6) The imperative need for large additional deliveries of natural gas to meet the requirements of the Rocky Mountain area, primarily those of domestic customers, will be satisfied without further unnecessary delay without any increase in present rates to the consumer.

> "These, then, are the principal reasons which lead us to issue our certificate order of March 1, 1951. Viewing dispassionately all of the evidence in this case, we think that denial of the application would have been a distinct disservice to the public" (R. 318-319).

The majority then imposed the condition which prompted reversal by the Court below.[6] This condition provided (10 F. P. C. 780):

> "* * * if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pursuant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers" (R. 269).

One Commissioner dissented on the granting of the certificate and, *inter alia*, objected that the condition sought

[6] In addition to the condition on gasoline operations the Commission imposed a further rate condition in this certificate proceeding providing as follows:

> "Colorado shall tender to all of its resale customers service agreements in which Colorado will agree * * * that it will not propose any increase in any rate subject to the jurisdiction of the Commission which will be attributable in whole or in part to the acquisition and merger authorized herein."

by the execution of the certificate condition. That court also recognized that in view of this public interest, natural-gas companies are not free to commit themselves in any unfettered fashion (R. 271). Colorado's action in regard to the condition therefore was immaterial.

Any obligation of a consensual nature has imported into it the overriding public policy of protecting both the public and the investor. This is the scheme of the Natural Gas Act which provides for the changing of a contract by Commission order. Under Section 5(a) it is expressly provided that the Commission, after hearing, "shall determine the just and reasonable rate * * *, or contract to be thereafter observed and in force, and shall fix the same by order * * *" *Cf. Addyston Pipe & Steel Company* v. *United States*, 175 U. S. 211, 228 (1899); *Louisville & Nashville Railroad Company* v. *Mottley*, 219 U. S. 467 (1911). But also the obligation of the Commission under the Act is to allow rates which in result are just and reasonable regardless of contract or other commitment. The process involves "a balancing of the investor and the consumer interests". *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U. S. 591, 602-603 (1944). The provisions of the Act, and not a party's consent to waive these provisions, control.

This brings up the point of waiver or acquiescence. In the first place, the nature of the case here for review must be considered. Colorado has not turned its back upon the condition to which it had consented. The court below held that the execution of that condition was not proper in this case since it had the effect of reducing what was determined to be a reasonable return. The Commission has not brought here the question whether that determination was correct or not. The only question here is whether the court below

to be imposed would be ineffective. This dissenter stated that he had serious question as to whether Colorado could be compelled to accept a confiscatory rate because of such condition.[7]

The certificate issued March 1, 1951. In its opinion issuing the certificate the Commission noted that the "future pattern" of Colorado's operations was settled and the rate case should proceed (R. 255-256, 10 F. P. C. 118). Accordingly on October 1, 1951 the hearings began on the rate case. On August 8, 1952, the Commission issued its order reducing Colorado's rates by $3,111,187 (R. 96-97). A part of this reduction was $878,202, which the Commission determined should be deducted from Colorado's cost of service. This was made up of $421,537 found by the Commission to be the loss on natural gasoline operations plus $456,665 of calculated income tax credit resulting from such asserted loss (R. 79, 127-128).

Colorado applied to the Commission for rehearing alleging, in relation to the natural gasoline question, that the Commission had not applied a method of allocating costs to this function which accorded with the condition and

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[7] The dissenting Commissioner stated:

> "These conditions, while devised to afford some protection to consumers against the natural consequences of the majority's action in approving the merger actually, in my opinion, have no such effect under the law. Should Colorado fail to earn a fair return in the future, the natural gasoline revenues given up to Southwestern cannot be treated as revenues of Colorado. They are gone forever. I question seriously whether the stockholders of Colorado can be compelled to accept a confiscatory rate of return simply because of a condition inserted in a certificate by the Federal Power Commission and accepted by their present Board of Directors. The present stockholders of Colorado, with the exception of Public Service, expect to distribute all of their holdings of Colorado's stock to the public as soon as the merger is consummated. The new stockholders will expect to be adequately compensated for their investment." (R. 311, note, 10 F. P. C. 133-134).

could make a decision at all—not whether the decision was correct. Colorado deems it entirely proper, therefore, to defend the right of the court below to consider the question. Otherwise this proceeding would be *ex parte*.[18]

United States v. Tucker Truck Lines, Inc., 344 U. S. 33 (1952), cited by the Commission, favors Colorado. There, this Court decided that a mere procedural irregularity, non-prejudicial in effect, is waived if timely objection is not made. Where the irregularity is more fundamental, waiver need not apply. This Court stated:

> "The question not being foreclosed by precedent, we hold that the defect in the examiner's appointment was an irregularity which would invalidate a resulting order if the Commission had overruled an appropriate objection made during the hearings. But it is not one which deprives the Commission of power or jurisdiction, so that even in the absence of timely objection its order should be set aside as a nullity" (344 U. S. at 38).

It is evident that where more than a mere personal right of a party (see Justice Frankfurter's dissent, 344 U. S. at 39) is involved, waiver is not readily declared.

Here, there was more than a procedural irregularity or personal right. A reduction of a just return involves fundamental public rights bearing upon the Constitutional issue of confiscation. Indeed, waiver under such circum-

[18] Any rule of preclusion arising from the acceptance of a benefit (see Com. Brf., p. 23) has no relevancy here. As is pointed out herein, the public interest transcends the conscious acceptance of that which is against the public interest. The record shows that the Commission was moved by public need in granting the certificate—not advantage to Colorado divorced from such need.

that the factors of the allocation method were missing. In the rehearing application, specific point was made of the fact that the Commission's treatment amounted to a reduction in the rate of return. This came about from the fact that the calculated tax saving had the effect of reducing the return from 5.75% purported to be allowed to 5.01% (R. 98-103, 106-114).[8]

The application was denied on this question. If the Commission had allowed an income tax associated with the return purportedly allowed, Colorado would have been entitled to an additional $456,665 (R. 112-114). In denying this, the Commission said:

> "Colorado alleges that it has been deprived of the rate of return to which it is entitled by reason of our treatment of the loss on gasoline operations in computing income taxes. Colorado claims the federal income tax allowance is properly calculated at $642,264, whereas our allowance is $185,599, or a difference of $456,665.
>
> "The difference between the claimed income tax liability and the income tax allowance we provided is the result of our treatment of the loss on gasoline operations of $421,537. We have found that the loss on gasoline operations should not be considered a part of the cost of service and with this finding Colorado does not take issue. Colorado would have us compute its federal and state income tax liabilities on the basis of earnings which do not reflect a reduc-

[8] The deduction of the loss plus the tax saving reduced the rate of return to 4.19%. The cost of service, as found by the Commission, including return purported to be allowed at 5¾% without any gasoline loss and tax saving, was $15,844,469 but that actually allowed was $14,952,567 (R. 80). The difference is $891,902 (this includes $13,709 of state taxes not shown above, see Com. Ref., p. 6). The rate base allowed was $57,048,988 (R. 53) and the rate of return at 5¾% (R. 69) is $3,280,317 (R. 80). The actual return after deducting $891,902 is $2,388,415 which when divided by the rate base of $57,048,988 equals 4.19% instead of 5¾%.

this rate case. It is evident that both were hard fought cases.[15] Serious consideration of the issues must, therefore, be assumed. In the certificate case the rate implications were without question considered, including, as mentioned, the validity of the gasoline condition.

With these facts, it is evident that the policy of such limitations as those contained in Section 19(b) has been satisfied. This policy, as announced by this Court, is quoted by the Commission as follows:

> "The agency charged with administering the Act should have the opportunity to 'consider the matter, make its decision, and state the reasons for its action' (*Unemployment Compensation Commission* v. *Aragon*, 329 U. S. 143, 155; 'orderly procedure and good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts' " (Com. Brf. pp. 31-32).

The announced salutary policy has been satisfied here through the interrelated certificate and rate proceedings and the express specific consideration in the former of the validity question.

C. The nature of the question is excuse for failure to raise.

1. The public interest.

The function of a "natural-gas company" is affected with a deep public interest. Section 1(a) of the Natural Gas Act so provides. The court below expressly recognized that important fact and upon the basis of it, refused to allow the reduction of a reasonable rate of return

[15] The majority of the Commission noted an adversary stand taken by its Staff. *In the Matter of Colorado Interstate Gas Company*, 10 F. P. C. 105, 106 (1951).

stances would appear to be totally immaterial. *Tucker*, therefore, supports what the court below did in this case.[17]

2. The fundamental importance of the issue.

The court below discovered and corrected substantial error leading to an unjust end result depriving Colorado of earning a fair return (R. 300). Under both the Constitution and the Natural Gas Act, it is apparent that rates set may not be unreasonable or confiscatory in their end result. *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U. S. 602, 603, 607 (1944).

The Commission does not seriously question that the substantive determination below was correct.[18] It is apparent that the court below would not permit the Commission to execute the condition in such a way as to give an illegal result. The court dealt with the Commission's power so to

[17] The Commission also cites *Helvering* v. *Wood*, 309 U. S. 344 (1940), and *United States, et al.* v. *Hancock Truck Lines, Inc.*, 324 U. S. 774 (1945). These cases are clearly distinguishable.

In *Helvering*, the Commissioner attempted in the Supreme Court to base an argument on another section of the Internal Revenue Code which had not been previously injected, but on the contrary, there had been an express waiver of reliance upon any section other than that expressly mentioned. The Court put great reliance upon this express waiver and would not permit the argument to be made before it for the first time.

In *Hancock*, there had again been an express waiver but in this case it related to a restriction in a certificate of public convenience and necessity permitting the appellee to serve only freight forwarders. This Court put great emphasis upon the express waiver.

There was not involved in either case a fundamental public right or question which goes to the power of the administrative agency under the organic law.

[18] The Commission admits that this issue is not "strictly relevant" (Com. Brf. p. 36, note). The Commission asserts, however, that the condition's imposition was an appropriate "balancing of the investor and consumer interests" and therefore was fully consonant with the "end result" principle. It then cites an oversubscription of Colorado's stock. Suffice it to say, this oversubscription occurred four months before the rate determination (R. ex. 97). This isolated transaction certainly has no bearing whatso-

act. So considered, we may again turn to the language in the *Tucker* case to the effect where a matter goes to power or jurisdiction, a resulting determination can be set aside as a nullity, even in the absence of timely objection. Stated another way, since an administrative agency necessarily assumes the legality or constitutionality of its action, reasonable ground exists for not assigning as error action which is not within the Constitution or the agency's organic law. *Cf.* dictum in *American Power & Light Company* v. *Securities and Exchange Commission*, 141 F. 2d 606, 612-613 (1st Cir. 1944).

III.

The Court of Appeals did not upset the Commission's certificate determination in the merger case but merely exposed an error of law.

The Commission claims error for the further reason that what the court below did in effect left the merger outstanding without the condition, thereby infringing upon the Commission's administrative functions.[19] The leading case and that cited by the Commission on this point is *Federal Power Commission* v. *Idaho Power Company*, 344 U. S. 17 (1952). The *Idaho Power* case and the case at bar are not alike, and the former has no effect as precedent here. In the *Idaho Power* case the Commission issued a certificate of convenience and necessity and attached a condition which the Court of Appeals struck down, and in an amended judgment required the issuance of the certificate without the condition. This Court held that by the second judgment the Commission usurped an administrative function. In

[19] Colorado seriously doubts whether this issue is before the Court as being "fairly comprised" within the narrow question presented

the instant case, the Court of Appeals did nothing of the kind. It merely considered the condition and held that the execution of that condition could not be used as a device for reducing Colorado's return below that which had been found reasonable.

The court below did not exercise the authority of the Commission in a certificate matter, but merely laid bare an error of law fully consistent with the holdings of this Court. This was fully consistent with the pronouncements of this Court in the *Idaho Power* case. The court below left to the Commission whatever action or consequences may follow so far as the merger certificate is concerned. At least, in not going further than laying bare the error of law, the court left the Commission free to do whatever else was necessary. The court below did not tell the Commission what it should do as to the certificate. Therefore, the normal rule should apply that the judgment will be the basis of whatever action the Commission might take. *Federal Power Commission* v. *Pacific Power & Light Company*, 307 U. S. 156, 160 (1939).

The Commission argues that the court below did more than lay bare an error of law even in view of the fact that the remand to the Commission was merely to make an appropriate rate adjustment in accordance with the opinion. The court below did not attempt to determine the status of the merger certificate without the condition. The Commission admits, however, that a "superficial argument may perhaps be made that the *Idaho Power* line of cases supports the court's ruling rather than the Commission's position" (Com. Brf. p. 52). This argument is made on the basis that the court below was not acting on a review of the certificate order and, therefore, was without authority to direct reconsideration of that order. This argument, of course, overlooks the fact that the court below gave no such

direction. The court below did merely lay bare an error of law. The Commission can do whatever it is free to do under the Natural Gas Act if the condition was truly a condition to the granting of a certificate; presumably the condition has failed, and if the Commission is so inclined, it may consider that Colorado is operating without a certificate and it can bring whatever proceedings it deems necessary under the Natural Gas Act to enjoin such unauthorized operations.

The Commission's argument is very strained and tenuous on this point. The impression is given that the merger condition was a substantial reason for granting the certificate. Whether this is so, depends upon subjective considerations. The record shows, however, that the Commission awarded the certificate for specific recited reasons which, as the Commission said (*supra*, pp. 6-7), "demonstrate succinctly the desirability of the project laid before us for judgment". Among these were the low cost of the merger to Colorado with a possible resultant cash benefit; the aquisition by Colorado of legal title to valuable natural gas reserves; the acquisition of valuable reversionary rights; a simple corporate structure with resultant savings; that there would result a financially sound company able to finance present and future expansions to meet consumer needs; and that there was an imperative need for large additional deliveries of natural gas to meet primarily the needs of domestic customers which would be satisfied without unnecessary delay and "without any increase in present rates to the consumer". The Commission then concluded: "These, then, are the principal reasons which lead us to issue our certificate order of March 1, 1951. Viewing dispassionately all of the evidence in this case, we think that denial of the application would have been a distinct "s-

Additionally, it must be borne in mind that the Commission's own counsel argued the ineffectiveness of the condition as a means for reducing Colorado's return (R. 311-312, note). The Commission must have acted with this advice in mind and must be assumed to have acted with a view to the possibility that the condition would be declared invalid. One of the Commissioners dissented from the granting of the certificate and stated his serious question whether Colorado stockholders could be compelled to accept a confiscatory rate of return because of the condition (R. 311, 10 F. P. C. 133). It is apparent, therefore, that in their deliberations, the Commission must have been confronted by one of its own number with this possible invalidity.

It wasn't the operation of the condition which was the sole consideration, or even one of the recited considerations for granting the certificate when the Commission came to summarizing its conclusion. Significantly, one thing that did impress the Commission was the supply of additional service without any increase in "present rates". The case taken to the court below for review was not a rate increase but was a rate decrease case. It is difficult, therefore, to assume that the Commission would not have granted the certificate without the condition. If, however, it thinks the condition's removal has rescinded the certificate, it is free to act on that basis. The court has not told it otherwise, as was done in the *Idaho Power* case.

The Commission makes the additional point that the court below was not dealing merely with an error of law. The court below was dealing only with the question of whether a reduction of what is otherwise determined to be a reasonable rate of return is a proper function of the Commission under the Natural Gas Act. The court's determination in the substantive sense can mean no more

return is beyond the Commission's authority under the organic law. This is about as pure a legal conclusion as it would be possible for a court to come to in a rate review proceeding. Certainly, the court in such determination has not interfered with the responsibility centralized in the Commission of inquiring into the technical complexities of the rate determination. *See Bingham's Trust* v. *Commissioner of Internal Revenue*, 325 U. S. 365, 382 (Justice Frankfurter, concurring) (1945). Of course, even questions of law must arise from facts, for without facts there can be no question of law. It is apparent, however, that a determination of the sort made by the court below is as nearly a pure question of law as can arise from an administrative proceeding.

Further argument is made by the Commission that direct review of the certificate determination was possible —except for estoppel. The implication is that the action of the court below constitutes a collateral attack upon the certificate determination, in that the court below leaves the certificate standing without the condition and Colorado did not seek review of the certificate case. In the first place, collateral attack is not involved. *Res judicata* would not apply in this sort of administrative determination. *Niagara Mohawk Power Corporation* v. *Federal Power Commission*, 202 F. 2d 190, 198 (D. C. Cir. 1952) affirmed 347 U. S. 239 (1954). In addition, the condition involved here was a rate condition which did not immediately adversely affect Colorado. Colorado would be adversely affected only on the contingency of a future determination of loss in a rate case. Colorado contends that review under these circumstances is premature. *Rochester Telephone Corporation* v. *United States*, 307 U. S. 125, 130 (1939); *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U. S. 591,

analogy to *Idaho Power* stating that the condition there was "in a sense" not immediately operative since the transmission lines which were to carry government power had not yet been constructed. The construction of physical facilities under a plan contemplated in a certificate proceeding certainly is considerably different from a future rate case wherein the condition might or might not be operative depending entirely upon whether the Commission concluded that there was or was not a calculated loss on the gasoline operations.

IV.

The Administrative Procedure Act justified the Court below in considering the question.

The court below took the position that it had inherent power *sua sponte* to note basic erroneous legal conclusions adduced from the established facts and cited in support of this power Section 10 of the Administrative Procedure Act. It was the court's view, in particular, that "To hold that we are precluded from considering the legality or constitutionality of the action of an administrative agency based upon facts found by it and unchallenged in the reviewing court would seem to make nugatory and meaningless these clear and positive mandates of the Section" (R. 301-302, 209 F. 2d 734).

The Commission contends that the Administrative Procedure Act does not affect the requirements of Section 19(b) of the Natural Gas Act (Com. Brf. pp. 40-48) and, therefore, the court below committed error. In its criticism of the court below, the Commission argues that the court failed to take adequate account of various phrases in Section 10 of the Administrative Procedure Act which the Commission considers "indicate that the Administrative Procedure Act

judicial review of issues not timely raised before the administrative agency" (Com. Brf. p. 46). Quite apart from the general position taken by the court below that the issue had been before the administrative agency and the court, it may be questioned whether the language relied on by the Commission supports the proposition contended for. For example, the primary reliance of the Commission is on the phrase in the introductory clause of Section 10 "which expressly makes Section 10 inapplicable where 'statutes preclude judicial review'" (Com. Brf. p. 45). Conceding that this introductory clause makes Section 10(e) inapplicable to a certain category of cases, it seems perfectly clear from the legislative history of the Act that the phraseology "statutes preclude judicial review" was not intended to refer to statutory provisions relating to the *scope* of judicial review of an administrative action which is subject to review.[20] There may well be room for doubt

[20] The report of the Senate Judiciary Committee on the bill which became the Administrative Procedure Act (S. Rep. No. 752, 79th Cong. 1st Sess., reprinted in S. Doc. No. 248, 79th Cong., 2d Sess., pp. 185-231) makes the following comment on the phraseology "statutes preclude judicial review" in the introductory clause of Section 10:

> "Very rarely do statutes withhold judicial review. It has never been the policy of Congress to prevent the administration of its own statutes from being judicially confined to the scope of authority granted or to the objectives specified. Its policy could not be otherwise, for in such a case statutes would in effect be blank checks drawn on the credit of some administrative officer or board." S. Doc. No. 248, p. 212.

The report of the House Judiciary Committee (H. Rep. No. 1980, 79th Cong. 2d Sess., reprinted in S. Doc. No. 248, 79th Cong. 2d Sess., pp. 233-291) contains exactly the same comment and adds several sentences which make it even clearer that the statutory provisions referred to in the introductory clause of Section 10 are those which entirely preclude any judicial review of the administrative action in question:

> "* * * To preclude judicial review under this bill a statute, if not specific in withholding such review, must upon its face give clear and convincing evidence of an intent to withhold it. The mere failure to provide specially by statute

as to the exact bounds of the phrase "statutes preclude judicial review", but *Heikkila* v. *Barber*, 345 U. S. 229 (1953), shows that the area of debate over the meaning of "statutes preclude judicial review" is not where the Commission suggests and, in particular, does not affect the applicability of Section 10 of the Administrative Procedure Act to the present case. The holding in *Heikkila* was that Section 10 of the Administrative Procedure Act does not apply to deportation proceedings under Section 19 of the Immigration Act of 1917, 39 Stat. 889, because Section 19 falls within the category of "statutes [which] preclude judicial review" even though deportation orders are subject to attack by writ of habeas corpus. The significance of *Heikkila* in relation to the present case would appear to lie not in the conclusion reached, which is not applicable, but in the recognition given to the general effect of Section 10 in expanding the scope of judicial review. After noting evidence in the legislative history of the Administrative Procedure Act that Congress intended the excepted category of "statutes [which] preclude judicial review" to be a narrow one, the Court commented:

> "* * * The spirit of these statements together with the broadly remedial purposes of the Act counsel a judicial attitude of hospitality towards the claim that § 10 greatly expanded the availability of judicial review * * *" 345 U. S. at 232.

The Commission relies, however, on the argument that "the legislative history of the Act shows that it was not designed to upset requirements such as that embodied in Section 19(b) of the Gas Act" (Com. Brf., p. 46). While this does not deny that the requirements in Section 19(b) should now be read *in the light of* the Administrative Procedure Act, it should also be noted that the particular items

of legislative history to which the Commission calls attention (Com. Brf., pp. 46-47) do not support its argument. The quotation from the Senate Committee Report (S. Doc. No. 248, 79th Cong., 2d Sess., p. 289, fn. 21, quoted at p. 47) relates to the doctrine of the exhaustion of administrative remedies, which is not here involved. The quoted statement by Senator McCarran (S. Doc. 248, 79th Cong., 2d Sess., p. 311, quoted at pp. 47-48) related to the proper interpretation of "statutes preclude judicial review" and was intended to refer only to statutory provisions which deny *any* judicial review. *See Heikkila* v. *Barber*, 345 U. S. 229, 237, 239-40 (dissenting opinion by Mr. Justice Frankfurter). The other statements referred to by the Commission (Com. Brf., pp. 46, n. 23, and 48) are also fully consistent with the interpretation here contended for.[21] Thus it appears that the Commission is in error in treating as wholly inapplicable to the present case the general injunctions to reviewing courts contained in the Administrative Procedure Act.[22]

A Court of Appeals is not limited as the Commission indicates. The reviewing court may hold unlawful and set

[21] Indeed, the statement by Representative Gwynne to which reference is made (Com. Brf., p. 48) appears to provide affirmative support for the contention that "statutes [which] preclude judicial review" are those which permit no judicial review at all:

> "* * * This bill does not give a court review in any case where review is now precluded by statute. It simply clarifies and expands in some particulars the authority of the court in reviewing cases in which court review is not precluded by law * * *." S. Doc. No. 248, pp. 374-75.

[22] The Commission argues that it is not in keeping with the design for the review of administrative orders to expand the record by appendices after decision in the Court of Appeals (Com. Brf., p. 40, note 19). The appendices referred to showed only the early genesis of the condition (R. 289, 322-325) or that the question of enforceability of the condition had been considered (R. 311-312, notes). The essentials of the condition itself, and the certificate opinions (R. order (R. 247-248), were made part of the rate case record during

aside fundamental action and conclusions not in accordance with law and in so doing the whole record is available to it for discovering fundamental error. In this regard, the provisions of Section 10 of the Administrative Procedure Act would appear to impose requirements of judicial review beyond the requirements of the Natural Gas Act. *Cf. Pittsburgh Steamship Company* v. *National Labor Relations Board*, 180 F. 2d 731, 736 (6th Cir. 1950).

The Commission relies strongly on a line of cases represented by the *National Labor Relations Board* v. *Cheney California Lumber Company*, 327 U. S. 385 (1946). The *Cheney* case and those like it can be safely contrasted with the situation at bar here. In *Cheney* it certainly appeared that the Labor Board determinations were entered almost completely on default. Here, however, Colorado had put to the Commission the question of reducing its rate of return. The contention of the Commission that a reviewing court is held within the narrowest possible limits where an administrative order is challenged, regardless of the enactment of the Administrative Procedure Act, was pretty well settled by this Court in *National Labor Relations Board* v. *Pittsburgh Steamship Company*, 340 U. S. 498 (1951). There, this Court considered the effect of the Taft-Hartley Act and the Administrative Procedure Act upon a reviewing court's authority and stated (340 U. S. at 500): "The Court of Appeals has now held, in accordance with our own view, that the scope of review had been extended 'beyond the requirements of the Wagner Act' • • • and that in the light of the new requirements the record considered as a whole disentitled enforcement of the order."

Regardless of the authority of the court to consider the question without the benefit of the Administrative Procedure Act, it is apparent that the court's obligation to

consider the end result was expanded by the enactment of that legislation. The court did not depend entirely upon the Administrative Procedure Act to support it. It discharged a full judicial responsibility under all of the applicable law.

Conclusion.

For the foregoing reasons, the judgment of the court below should be affirmed to the extent that it has refused to permit the deduction from the proper rate of return pursuant to the certificate condition under which the Commission excluded from the cost of service of Colorado the losses from gasoline operations and an associated income tax credit.

Respectfully submitted,

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Appendix.

1. Section 19 of the Natural Gas Act (52 Stat. 821, 831, 15 U. S. C. (717r) provides in pertinent part:

> (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State, municipality or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. * * * No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.
>
> (b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing a written petition praying that the order of the Commission be modified or set aside in whole or in part. * * * No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. * * *

2. Section 10 of the Administrative Procedure Act (60 Stat. 237, 243, 5 U. S. C. (1009)

Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion——

* * * * * *

(e) SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of the agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.